88-1275

No. .....

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1988

LEWIS R. CRIST, RECEIVER FOR TRANSIT CASUALTY COMPANY,

Petitioner,

v.

WAL-MART STORES, INC. AND ALEXANDER AND ALEXANDER, INC.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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QUESTIONS PRESENTED

1. Whether the Eighth Circuit's application of the doctrine of *in pari delicto* against the Receiver of an insolvent workers' compensation carrier who was attempting to collect legal premiums based on the rating regulations of nineteen (19) states incorrectly destroys the national regulatory scheme developed in the area of workers' compensation and incorrectly permits a large company to deceive public authorities.

   a. Whether the Eighth Circuit incorrectly refused to extend the rationale of *D'Oench Duhme and Co. v. F.D.I.C.*, 315 U.S. 447 (1942), to public regulatory authorities in the insurance industry.

PARTIES TO THE PROCEEDING

The Petitioner Lewis R. Crist is the Receiver for Transit Casualty Company. Transit issued workers' compensation policies to Wal-Mart Stores for the years 1983-1984 and 1984-1985, through one of its local agents, Miro and Associates of Dallas, Texas. Transit was a Missouri Corporation with its principal place of business in Los Angeles, California.

The Respondent Wal-Mart Stores, Inc. is a large retail company which maintains its principal place of business in Bentonville, Arkansas. Wal-Mart purchased workers' compensation insurance from Transit through its own broker, Alexander and Alexander, Inc. Respondent Alexander and Alexander is a nation-wide insurance brokerage firm with its principal place of business in Kansas City, Missouri.

Jurisdiction in the district court was based on diversity of citizenship.

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

The petitioner, Lewis R. Crist, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Eighth Circuit, filed in the above-captioned proceeding on August 26, 1988.

OPINIONS

The Opinion of the Court of Appeals for the Eighth Circuit is reported at 855 F.2d 1326, and is reprinted in the appendix hereto, p. 2a, *infra*. The court's Order denying petitioner's Motion for Rehearing and Review En Banc is reprinted in the appendix hereto, p. 1a, *infra*. The Eighth Circuit's order was entered on November 18, 1988. The Opinion and Order of the United States District Court is reported at 664 F. Supp. 1242 (W.D. Ark. 1987), and is reprinted in the appendix hereto, p. 25a, *infra*.

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JURISDICTION

Respondent Wal-Mart Stores brought this suit in the United States District Court, Western District of Arkansas, based on diversity of citizenship. On July 6, 1987, the Western District granted judgment in favor of the petitioner on his counterclaim for $18,000,000.00. See p. 2a, *infra*.

On respondent's appeal, the Eighth Circuit on August 26, 1988, entered an opinion reversing the Western District's judgment for $18,000,000.00 and directing that both petitioner's and respondents' claims be dismissed based on the doctrine of *in pari delicto*.

Petitioner's Petition for Rehearing and Request for Review En Banc were denied on November 18, 1988.

The jurisdiction of this court to review the judgment of the Eighth Circuit is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Ala. Code § 27-12-14 (1975)

Ariz. Rev. Stat. Ann. § 20-449 (1975)

Ark. Stat. Ann. § 66-3019 (1977)

Fla. Stat. Ann. § 626.9541(1)(n) (West Supp. 1987)

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Miss. Code Ann. § 83-3-121 (1972)

Mo. Rev. Stat. § 379.356 (Supp. 1986)

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Neb. Rev. Stat. § 44-361 (1984)

Okla. Stat. Ann. tit. 36, § 1204 (1976)

S.C. Code Ann. § 38-55-130 (Law Co-op 1984)

Tenn. Code Ann. § 56-8-104(8) (1980)

Tex. Ins. Code Ann. § 21.21 § 4(8) (Vernon 1981)

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STATEMENT OF THE CASE

This is a declaratory judgment action brought by Wal-Mart Stores (hereinafter referred to as Wal-Mart) against Transit Casualty Company (hereinafter referred to as Transit) for a declaration that it owed no additional premiums on workers' compensation policies issued for the years 1983-1984 and 1984-1985. The policies provided workers' compensation coverage for Wal-Mart in nineteen (19) states. Wal-Mart contended that it owed no additional premium based on a "side agreement" which was negotiated with one of Transit's agents. The "side agreement" was not made part of the policy. Transit counterclaimed for over $18,000,000.00 in additional premium as calculated pursuant to the statutory requirements of the nineteen (19) states involved. Wal-Mart filed a Third-Party Complaint against its broker, Alexander and Alexander (hereinafter referred to as A & A), for indemnity on the Counterclaim of Transit. Transit was later declared insolvent and Lewis R. Crist of the Missouri Department of Insurance was appointed as Receiver and substituted as the defendant and counterclaimant.

On July 6, 1987, the United States District Court for the Western District of Arkansas issued an Opinion finding that the "side agreement" was illegal in all nineteen (19) states and entered judgment in favor of the Receiver for $16,772,144.00 plus prejudgment interest.[1] The district court concluded that the agent exceeded his actual authority in negotiating the illegal "side agreement", and

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[1] *Wal-Mart Stores, Inc. v. Crist,* 664 F. Supp. 1242 (W.D. Ark. 1987). See p. 25a, *infra*.

that Wal-Mart could not rely on apparent authority to enforce the "side agreement" because the evidence did not support a reasonable belief by Wal-Mart that the "side agreement" was legal when negotiated. See p. 66a, *infra*.

The district court further concluded that Wal-Mart, not the Receiver, was attempting to enforce an illegal agreement and that workers' compensation insurance is social insurance highly regulated by the states to the extent that all premiums are established by law. See p. 87a, *infra*. Therefore, the district court found that Wal-Mart was required to pay workers' compensation premiums to the Receiver as calculated pursuant to the policies actually issued and the appropriate regulatory requirements of the nineteen (19) states involved.

Finally, the district court refused to apply the doctrine of *in pari delicto* against the Receiver because Wal-Mart, not the Receiver, was attempting to enforce an illegal agreement, and because the defense is not available against a Receiver seeking to recover additional workers' compensation premium based on state regulations. See p. 86a, *infra*.

By opinion filed August 26, 1988, the United States Court of Appeals for the Eighth Circuit reversed the district court's judgment. See p. 2a, *infra*. The Eighth Circuit refused to permit the Receiver to recover additional premium because of the doctrine of *in pari delicto*. See p. 19a, *infra*. In accepting the repudiated doctrine of *in pari delicto* in regulatory cases, the Eighth Circuit ignored the special relationship that a Receiver of an insolvent insurance company holds to the public when attempting to enforce compliance with regulatory guidelines in the area

of workers' compensation insurance. The court also ignored the impact of such a far reaching opinion on the nineteen (19) states involved and the national regulatory scheme designed for the protection of workers injured on the job.

The Receiver's Petition for Rehearing and Consideration for Rehearing En Banc was denied on November 18, 1988. See p. 1a, *infra*. From these decisions, the present Writ of Certiorari is sought.

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REASONS FOR GRANTING THE WRIT

I.

THE EIGHTH CIRCUIT'S APPLICATION OF THE DOCTRINE OF IN PARI DELICTO TO DEFEAT A PUBLIC REGULATOR'S ATTEMPT TO ENFORCE THE REGULATIONS OF NINETEEN (19) STATES AND COLLECT LEGAL PREMIUMS WAS (A) CONTRARY TO PUBLIC POLICY CONSIDERATIONS, AND (B) CONFLICTS WITH EVERY DECISION ACROSS THE COUNTRY WITH RESPECT TO ENFORCEMENT OF UNIFORM PREMIUM REGULATIONS FOR WORKERS' COMPENSATION.

The United States Court of Appeals for the Eighth Circuit improperly applied the doctrine of *in pari delicto* against the Receiver of an insolvent workers' compensation insurance company who was seeking to collect $18,000,000.00 in legal premiums from a large insured as required by the regulatory authorities of nineteen (19) states. Although the Eighth Circuit acknowledged that

the "side agreement" contracted by an agent and the insured was illegal in all nineteen (19) states and that its specific design was to deceive state regulatory authorities, the court refused to enforce the statutory rates reflected in the written policy. See p. 18a, *infra*. Instead, the Eighth Circuit voided the policy, cancelled all coverage and refused to permit the Receiver to collect any of the $18,000,000.00 legally owed by Wal-Mart.

The Eighth Circuit's application of the doctrine of *in pari delicto* effectively destroys the regulatory scheme designed to ensure that all insureds, large and small, pay their fair share of premiums for workers' compensation coverage. The regulations sought to be enforced by the Receiver require that premium not be excessive, inadequate or discriminatory based on the size or economic power of the insured. See p. 18a, *infra*. The Eighth Circuit's used of *in pari delicto* against the Receiver is in direct conflict with the uniform regulatory scheme established in every applicable state and contrary to the decisions of all states faced with illegal workers' compensation premium agreements. See p. 71a, *infra*.

In January, 1983, Wal-Mart, A & A and Miro and Associates Risk Management (Miro), an agent of Transit Casualty Company, negotiated for the issuance of a workers' compensation policy to Wal-Mart for mandatory coverage in nineteen (19) states. At the time of the negotiations, Miro was an agent of Transit and A & A was serv-

ing as Wal-Mart's broker. A & A worked directly with John Sooter, Wal-Mart's very experienced risk manager.[2]

Following negotiations, Miro agreed to issue Wal-Mart a standard workers' compensation policy for a flat rate premium of $3,500,000.00 per year. In order to make it appear to satisfy state regulatory requirements, Miro issued a policy which reflected false payroll amounts and appeared on its face to correctly calculate premium by multiplying actual payroll times state regulated rates and the application of an experience modifier promulgated by the National Commission on Compensation Insurance (hereinafter referred to as NCCI). All states, including the nineteen (19) involved with Wal-Mart, required compliance with this formula to ensure that workers were adequately protected. See pp. 16a and 73a, *infra*. All workers' compensation policies are based on estimated payrolls which are thereafter audited at the end of the year. If, based on an audit of payroll, the insured owes additional premium, it is collected at year end. This method of computing workers' compensation premium is standardized throughout the nation. See p. 73a, *infra*.

The illegal "side agreement" entered into between Wal-Mart, A & A and Miro did not consider these regulatory requirements. See p. 18a, *infra*. The agreement was an oral agreement which gave Wal-Mart coverage in nineteen (19) states for a flat premium of $3,500,000.00 re-

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[2]The evidence revealed that Wal-Mart had been self-insured for several years preceding the negotiations and had extensive experience with the concepts involved in workers' compensation premium regulation. Further, A & A provided full-time professional advice to Wal-Mart concerning workers' compensation matters. See p. 68a, *infra*.

gardless of payroll. See p. 17a, *infra*. The "side agreement" was designed to deceive both the company and state regulatory authorities. See p. 17a, *infra*. Instead of sending the proposed "side agreement" to regulatory authorities, Miro issued a standard policy which contained false payroll figures. Wal-Mart received a copy of the policy knowing that it was false.

A year end audit of payroll revealed that Wal-Mart owed over $6,000,000.00 in additional premium for the initial policy period. Transit ordered Miro to bill the additional premium pursuant to statutory requirements. In order to satisfy the statutory requirements, Miro and Wal-Mart designed a scheme whereby Wal-Mart would wire transfer $6,000,000.00 to Miro who would immediately notify Transit and state regulatory authorities (falsely) that the additional premium had been paid. After notification, Miro would wire transfer the $6,000,000.00 back to Wal-Mart to complete the circle of deception. See p. 67a, *infra*. The intent of the scheme was to deceive both Transit and state regulatory authorities. See p. 69a, *infra*.

Workers' compensation premium development is highly regulated by every state because workers' compensation insurance is social insurance which every employer is required to obtain. See p. 71a, *infra*. All nineteen (19) states referenced in Wal-Mart's policies have extensive regulations for the computation of premium.[3] Both the

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[3]*See, Ala. Code* § 27-12-14 (1975); *Ariz. Rev. Stat. Ann.* § 20-449 (1975); *Ark. Stat. Ann.* § 66-3019 (1977); *Fla. Stat. Ann.* § 626.9541(1)(n) (West Supp. 1987); *Ga. Code Ann.* § 33-9-36 (1982); *Ill. Ann. Stat.* ch. 73, ¶ 763 (1965); *Ind. Code Ann.* § 27-1-

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district court and the Eighth Circuit found Wal-Mart's "side agreement" in violation of the law of every applicable state and therefore unenforceable. See p. 18a, *infra*. The finding of illegality was consistent with every decision from all jurisdictions faced with "side agreements" contrary to uniform premium regulation.[4]

The district court refused to permit Wal-Mart to benefit from this illegal scheme by asserting the defense of *in pari delicto* against the Receiver in his claim for additional premium. The district court reasoned that the very purpose of the rule of *in pari delicto* would be defeated if Wal-Mart were permitted to successfully circumvent state regulations by enforcing the "side agreement" against the Receiver. See p. 87a, *infra*. Further, the district court noted that every case from other jurisdictions

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20-30 (Burns 1986); *Iowa Code Ann.* § 507B.4 (Supp. 1987); *Kan. Stat. Ann.* § 40-041 (1986); *Ky. Rev. Stat. Ann.* § 304.12-090 (1980); *La. Rev. Stat. Ann.* § 22-1214 (West 1978); *Miss. Code Ann.* § 83-3-121 (1972); *Mo. Rev. Stat.* § 379.356 (Supp. 1986); *Neb. Rev. Stat.* 44-361 (1984); *N.M. Stat. Ann.* § 59-16-15 (1978); *N.C. Gen. Stat.* § 58-44.5 (1982); *Okla. Stat. Ann* tit. 36, § 1204 (1976); *S.C. Code Ann.* § 38-55-130 (Law Co-op 1984); *Tenn. Code Ann.* § 56-8-104(8) (1980); *Tex. Ins. Code Ann.* § 21.21 § 4(8) (Vernon 1981).

[4]*See, American Mutual Liability Ins. Co. v. Plywood-Plastics Corp.*, 81 F. Supp. 157 (E.D. S.C. 1948); *Key System Transit Lines v. Pacific Employers Ins. Co.*, 345 P.2d 257 (1959); *Contractors' Safety Assoc. v. California Comp. Ins. Co.*, 307 P.2d 626 (1950); *Warm Springs Forest Products Ind. v. Employee Benefits Ins. Co.*, 703 P.2d 1008 (1985), *aff'd* 716 P.2d 740 (1986); *Mountain Fir Lbr. Co. v. E.B.I. Co.*, 679 P.2d 296 (1984); *Biggs v. Reliance Life Ins. Co.*, 195 S.W. 174 (Tenn. 1917); *Associated Employers Lloyds v. Dillingham*, 262 S.W.2d 544 (Tex. Civ. App. 1953); *Glenn H. McCarthy, Inc. v. Knox*, 186 S.W.2d 832 (Tex. Civ. App. 1945); *Employer's L.A. Corp. v. Success-Uncle Sam Conc. Co.*, 208 N.Y.S. 510 (1925).

concerning enforcement of workers' compensation premium regulations refused to apply *in pari delicto* because states had taken the ability to bargain away from employers with respect to workers' compensation premium development and that all employers, large and small, were required by law to pay their fair share of premiums. See pp. 71a-72a, *infra*. Finally, the district court refused to apply the doctrine of *in pari delicto* against the Receiver because Wal-Mart, not the Receiver, was attempting to enforce an illegal contract. The Receiver was relying on legal state regulations and the written policy issued and accepted by Wal-Mart. The district court correctly recognized that the application of *in pari delicto* would defeat the very purpose of state regulations. See p. 87a, *infra*.

A Receiver, such as Mr. Crist, is bound to administer the insolvent's estate on behalf of the claimants, creditors and other parties interested in its assets. *Mo. Rev. Stat.* 375.670. Therefore, a Receiver represents not only the insolvent company's interests, but also those of its claimants and creditors, such as injured employees of the insured. Those creditors and claimants are the "innocent parties" who will be hurt by the deception inherent in "side agreements". As a representative of those innocent creditors, Mr. Crist should not be bound by any actions taken by Transit's agents prior to his appointment, where those actions violate the law and public policy of nineteen (19) states. Whatever the evidence shows as to Transit, the Receiver is not *in pari delicto* with Wal-Mart.[5]

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[5]The district court did not reach the issue of whether to apply the doctrine of *in pari delicto* against the Receiver be-

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The recognition of a distinction between the acts of an insolvent and a Receiver has long been the rule applied in receiverships for failed financial institutions. *D'Oench Duhme and Co. v. F.D.I.C.*, 315 U.S. 447 (1942). The *D'Oench* doctrine holds that, because "side agreements" vary the terms of a contract, they deceive examining regulatory authorities and negate the purposes of regulation. They are unenforceable against Receivers of failed banks, and the agreement which appears in the bank records to be relied upon by bank examiners must be enforced. In this context, the intent of the contracting parties to controvert the law is of no effect. *See also, F.D.I.C. v. Van Laanen*, 769 F.2d 666 (10th Cir. 1985); *F.D.I.C. v. Investors Associates*, 755 F.2d 152 (6th Cir. 1985); *F.D.I.C. v. First National Finance Co.*, 587 F.2d 1009 (9th Cir. 1978); *F.D.I.C. v. First Mortgage Investors*, 485 F.Supp. 445 (E.D. Wis. 1980). The *D'Oench* doctrine prevents any party from taking advantage of the deception inherent in "side agreements". It allows regulators to rely upon their examination of company records for an accurate reflection of the company's financial condition and status.[6]

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cause of the numerous opinions from state courts in non-receivership cases which refused to permit the defense when asserted to defeat a claim for statutory premium. See p. 81a, *infra*. The Eighth Circuit applied the rule despite the numerous state decisions, and then refused to recognize the special relationship between the Receiver and the public in permitting the defense to be used to defeat the Receiver's attempt to enforce the regulations. See p. 21a, *infra*.

[6]In *Firstsouth, F.A. v. Aqua Const., Inc.*, 858 F.2d 441 (8th Cir. 1988), the Eighth Circuit extended *D'Oench* to the FSLIC on the basis that federal common law would by analogy adopt the same protection afforded to the FDIC.

In *D'Oench,* the United States Supreme Court held that the maker of a secret "side agreement" was estopped from utilizing it as a defense against a Receiver's action to enforce a note. It found that the act of giving the "side agreement" "contravenes a general policy to protect the institution of banking from such secret agreements." *D'Oench, supra,* at 458. By allowing Wal-Mart to use a "side agreement" to escape liability under the standard workers' compensation policy issued to it, the Eighth Circuit ignored the general public policy of protecting injured workers by ensuring that insurance carriers were financially sound enough to pay claims.

The public policy considerations forming the basis for the *D'Oench* rule have long been applied in the insurance industry. *Glenn H. McCarthy, Inc. v. Knox,* 186 S.W.2d 832 (Tex. Civ. App. 1945). In *McCarthy,* the Receiver for an insolvent insurance company filed suit against an insured to recover additional premium on a workers' compensation policy alleging that the carrier and insured illegally contracted for a premium less than the rates on file with the insurance department. The "side agreement" was not made part of the policy issued and was not submitted to the insurance department for approval. The Texas Court of Civil Appeals ordered payment of additional premium and refused to enforce the illegal "side agreement." In doing so, the court recognized that workers' compensation rates are fixed by law and that insureds are charged with knowledge of the rates on file. The court further held that the rates promulgated by the commission are not subject to alteration by

agreement, waiver, estoppel, *in pari delicto* or any other affirmative defense.[7]

The Eighth Circuit incorrectly used the doctrine of *in pari delicto* against the Receiver and totally ignored the numerous sound decisions from other jurisdictions which were previously on point. The court, although finding the "side agreement" illegal in all nineteen (19) states, totally ignored the vital public interest involved in the uniform regulation of workers' compensation premium development and essentially destroyed the regulators' ability to correct deceptions perpetrated against state regulatory authorities. The panel's decision is contrary to all existing precedent and defeats the purpose of discouraging deception against public regulators.

In reversing the Judgment of the district court, the Eighth Circuit refused to extend the rationale of the *D'Oench* rule outside of the banking industry and ignored existing case law in the area of workers' compensation which applied the *O'Dench* principle. The *D'Oench* rule should be applied in insurance receiverships for the same reasons it is applied in bank receiverships. It is designed to assist public regulators in the enforcement of regulations. The rule recognizes that public regulators represent the public and should not be bound by illegal acts of company officials or agents when reviewing and examining companies like Transit.

The social nature of workers' compensation insurance requires that regulators have full authority to seek mone-

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[7]This strong policy consideration has been applied in every state court faced with the issue of enforcement of workers' compensation regulations. See cases cited in footnote 3, *supra*.

tary recovery from participants in illegal agreements without having to overcome the defense of *in pari delicto*. This is especially true when the deception complained of is deception against public authorities charged with the responsibility of ensuring that adequate premiums are charged and collected for workers' compensation insurance. The Eighth Circuit's analysis ignores the significant public interest in regulating workers' compensation insurance. Insurance for job related injuries is an issue of vital public concern and the parties' relative fault should play no part in the decision-making process where the Receiver, as a representative of the public, is seeking to ensure compliance with state laws.

In order to protect the ability of states to regulate the insurance industry and to help prevent future insolvency, the deception inherent in "side agreements" should not be allowed.[8] The Eighth Circuit's decision has created mass confusion among state regulatory authorities and has jeopardized any attempt to uniformly regulate workers' compensation for the benefit of the public. State insurance departments across the country are now left with very stringent underwriting regulations for work-

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[8]Following insolvency, guarantee funds throughout the country were required to accept Transit's liability on "covered" claims. Numerous claims were paid by the guarantee funds prior to the Eighth Circuit's opinion. As a result of the opinion, responsibility for payment was shifted to Wal-Mart because the Eighth Circuit found the *coverage* term of the policies void. As a result of this finding, Wal-Mart did not have to pay additional premium or pay losses because state guarantee funds, which relied on the existence of coverage, had paid injured workers millions of dollars. The Eighth Circuit permitted Wal-Mart to have free coverage at the public's expense.

ers' compensation but no means to enforce them where a secret "side agreement" has been negotiated.

In *Pinter v. Dahl,* 486 U.S. —, 100 L.Ed.2d 658 (1988), the Supreme Court recognized that the doctrine of *in pari delicto* has traditionally required that public policy implications be carefully considered before the defense is allowed. If application of the rule does not offend underlying public policy considerations, the defense may be used. However, if application of the rule destroys the very purpose of the rule and permits one to achieve the goal of circumventing regulations, the defense has no applicability. In the present case, as a result of the Eighth Circuit's application of *in pari delicto,* Wal-Mart has achieved its goal of circumventing state regulation of premium. It has avoided paying statutory premium; it has avoided paying its injured workers; and it has profited at the expense of state funds across the country.

For the reasons set forth above, the Petitioner requests that its Petition for Writ of Certiorari be granted.

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CONCLUSION

The Eighth Circuit's application of the doctrine of *in pari delicto* against the Receiver was improper and has devastated all attempts to uniformly regulate workers' compensation premium development. The decision is contrary to every reported case concerning workers' compensation premium regulation and is a matter of utmost con-

cern to every state regulator. The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 87-2212-WA

Wal-Mart Stores, Inc.,	)	
	)	
Appellant,	)	Appeal from the
	)	United States
vs.	)	District Court for
	)	the Western Dis-
Lewis R. Crist, et al.,	)	trict of Arkansas
	)	
Appellees.	)	

Appellee Lewis R. Crist petition for rehearing en banc has been considered by the Court and is denied.

Judges Heaney and McMillian would have granted the petition. Judges John R. Gibson and Magill did not participate.

Petition for rehearing by the panel is also denied.

November 18, 1988

Order Entered at the Direction of the Court:

Robert D. St. Vrain

Clerk, United States Court of Appeals, Eighth Circuit

WAL-MART STORES, INC., Appellant,

v.

Lewis R. CRIST, Appellee.

WAL-MART STORES, INC., Appellant,

v.

ALEXANDER &
ALEXANDER, Appellee.

No. 87-2212.

United States Court of Appeals,
Eighth Circuit.

Submitted May 9, 1988.

Decided Aug. 26, 1988.

Rehearing and Rehearing En Banc Denied

Nov. 18, 1988.

Insured under workers' compensation policy filed declaratory judgment action seeking enforcement of agreement entered into with agent of insurer under which it was to be provided coverage for all of its employees in exchange for $3.5 million premium. Insurer counterclaimed for nearly $20 million in additional premiums allegedly due. The United States District Court for the Western District of Arkansas, 664 F.Supp. 1242, H. Franklin Waters, Chief Judge, determined that corporation was liable for sum of $19.9 million in additional premiums under standard rates in policy if applied to corporation's actual payroll. Corporation appealed. The Court of Appeals, Beam, Circuit Judge, held that: (1) insurer's agent did not have actual authority to enter into agreement

utilizing premium rates not on file with appropriate state regulatory agencies; (2) agent had apparent authority to enter into transaction; (3) premium agreement violated state law by misrepresenting information required by law to be reported truthfully in every state; (4) both parties to transaction were in pari delicto and thus no relief could be accorded either; and (5) corporation bore ultimate responsibility for payment of any workers' compensation claims remaining unsatisfied.

Affirmed in part, reversed in part and remanded with directions.

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David A. Ranheim, Minneapolis, Minn., for appellant.

William H. Sutton, Little Rock, Ark. and Philip J. Walsh, New York City, for appellee.

Before WOLLMAN and BEAM, Circuit Judges, and RE,* Chief Judge.

BEAM, Circuit Judge.

Wal-Mart Stores, Inc. (Wal-Mart) appeals from a district court ordering it to pay $19,946,038.20 in premiums and interest to the receiver of an insolvent insurance carrier, Transit Casualty Company (Transit), which carrier issued policies of workers' compensation insurance covering Wal-Mart employees in the states in which Wal-Mart conducted business. Wal-Mart contends that the district court drew erroneous legal conclusions from certain un-

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* The HONORABLE EDWARD D. RE, Chief Judge, United States Court of International Trade, sitting by designation.

disputed facts presented over seven days of trial. We agree and reverse.

BACKGROUND

The facts of this case are lengthy and complex. The district court issued an opinion which sets forth the numerous transactions giving rise to this litigation, see *Wal-Mart Stores, Inc. v. Crist,* 664 F.Supp. 1242 (W.D.Ark. 1987), and we will not attempt to restate each of the district court's findings here. We will, however, discuss those facts essential to an understanding of the issues presented on appeal and to our resolution of those issues.

Wal-Mart owns and operates a very successful chain of retail stores, with facilities in eighteen states at the times relevant to this appeal. In each of these states, as required by law, Wal-Mart provided workers' compensation insurance for its employees. Begining in 1980, Wal-Mart became self-insured for its workers' compensation obligations and for its general liability risks in all states in which it conducted business except Texas and a few southern states in which it maintained only a limited number of employees. Wal-Mart remained self-insured through late 1982, at which time John Sooter, Wal-Mart's Director of Risk Management, sought proposals for renewal or replacement of the workers' compensation policy covering Wal-Mart's Texas employees. Offers were solicited through Wal-Mart's insurance consultant, Alexander & Alexander (A & A). One of the quotes which A & A presented to Wal-Mart was from Transit through its agent Carlos Miro.

Carlos Miro owned and operated Miro & Associates, an underwriting agency in Dallas, Texas. In May of 1982, Miro entered into a "Managing Agency Agreement" with Donald F. Muldoon & Co., Inc. (Muldoon), a Transit general agent who possessed authority to appoint sub-agents. This agreement authorized Miro to issue and place insurance coverage on Transit's behalf. Miro was provided with blank Transit policy forms for this purpose, and quickly became Transit's most productive agent.

The quote which Miro provided for Wal-Mart's Texas workers' compensation coverage, utilizing Transit policy forms, was quite favorable. Upon receipt of the Texas proposal, Wal-Mart asked Miro to provide a quote for workers' compensation coverage for all Wal-Mart employees to replace the self-insurance arrangement utilized by Wal-Mart in the other states. Miro gladly accepted Wal-Mart's invitation, obtained and reviewed Wal-Mart's payroll data and loss history for several prior years, and arranged a meeting in Dallas to present his proposal.

Miro offered to provide workers' compensation insurance coverage for all Wal-Mart employees for a flat and guaranteed premium of $3,500,000.00. The premium was to be unaffected by any factor other than an increase or decrease in Wal-Mart's estimated annual payroll, a change in which would increase or decrease the premium proportionately. The district court found, though Miro did consider Wal-Mart's loss history in reaching the $3.5 million figure, that Miro quoted the premium as a guaranteed flat rate, not to be adjusted or influenced by the amount of

claims paid.[1] This arrangement was very attractive to Wal-Mart, according to Sooter, not only because of the competitive price, but because Wal-Mart could budget in advance for a fixed maximum premium expense. Wal-Mart accepted Miro's bid, and received a cover note and binder from Miro which set forth the terms of the agreement.[2]

Somewhere between thirty and sixty days after the coverage took effect, Miro sent A & A the Transit policy which purportedly embodied the agreement. A & A reviewed the policy, considered it satisfactory, and sent it to Wal-Mart who also reviewed its terms. The policy contained a provision for computation of premium in accordance with standard manual rates promulgated by the National Council of Compensation Insurers, which rates were on file with the appropriate state regulatory bodies. The various rates were multiplied by estimated payroll

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1. Miro's proposal did include a formula, which would have adjusted the premium downward if Wal-Mart were to have an extremely favorable loss experience. However, the district court found, and we agree, that even with this potential adjustment, the parties all understood the principal element of the proposal to be a maximum guaranteed premium which would not be increased if losses became substantial.

2. Miro also agreed to provide coverage for Wal-Mart's future liability for workers' compensation benefits for the period from February 1, 1980 through January 31, 1983, when Wal-Mart was self-insured. This coverage was provided for just under $3 million, the amount of reserves which had been established by Wal-Mart on claims incurred and reported during this period. With respect to this agreement, involving "tail coverage" as the district court described it, the district court found that Miro and Wal-Mart had entered into a fully enforceable agreement which was binding upon both parties. This portion of the district court's decision is not challenged on appeal, and we shall not discuss it further.

for each job classification to reach an aggregate premium. The policy was structured so that the premium obtained after multiplication of rates times payroll, less discounts, was exactly $3,500,000.00, as agreed upon. However, to reach this result, Wal-Mart's estimated payroll, reported by Transit to be $547,000,000.00, was reduced on the face of the policy to approximately $250,000,000.00. If the actual payroll estimate had been used, the total premium due would have been well in excess of the agreed upon figure. Wal-Mart and A & A were both aware that the estimated payroll had been depressed, but took no action and accepted the policies. In fact, A & A advised Wal-Mart that this was a common practice in the insurance industry and that it should be of no concern. Additionally, certain endorsements were attached to the policy which, if enforced, would have operated to raise the premium if losses proved greater than expected. Wal-Mart and A & A were also aware of these provisions, but apparently assumed they would not be enforced, since to do so would violate the premium portion of the agreement. A similar policy was issued for the following year, for the same $3.5 million maximum premium. Payroll figures utilized in the renewal policy were also substantially depressed.

Near the end of the second policy year, problems began to surface. Claims on the Wal-Mart policies turned out to be well beyond any of the parties expectations, and far in excess of premiums collected on the policies. Transit asserts that amounts paid to date on the two policies approximate $21,000,000.00. It is not surprising therefore, that Transit soon learned that Miro's captive rein-

surers, with whom the entire risk on the Wal-Mart policies had been reinsured, had stopped paying claims.[3] Shortly thereafter, Miro's agency with Transit was terminated, and Transit demanded additional premium payments from Wal-Mart in accordance with the rates set forth in the issued policies and Wal-Mart's actual payroll.

Upon receipt of Transit's demand for additional premium, Wal-Mart filed this suit for a declaratory judgment seeking enforcement of the agreement entered into with Miro. Transit answered, alleging that the agreement which Wal-Mart seeks to enforce is contrary to law and unenforceable. Transit also counterclaimed for nearly $20,000,000.00 in additional premiums it claims Wal-Mart owes pursuant to the terms of the two policies. Wal-Mart denied liability on the counterclaim, and filed a third-party claim against A & A, seeking recovery of any amounts which Wal-Mart is required to pay to Transit. After making thorough and detailed factual findings, the district court concluded (1) that Miro exceeded his authority, both actual and apparent, in entering into the agreement with Wal-Mart; (2) that the premium provisions of the agreement are illegal and unenforceable under state insurance law; and (3) that Wal-Mart is bound by the terms which were actually embodied in the Transit policies, though those terms differ substantially from

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3. The Wal-Mart policies had been 100% reinsured through offshore captive reinsurance companies under Miro's control. Transit had made a conscious effort to expand its involvement in such offshore captive reinsurance ventures, in which Transit served merely as the "fronting" company, permitting the use of its policy forms for a percentage fee. Assuming all risks were properly reinsured with solvent companies, Transit believed it was protected from exposure on the insured risks.

the actual agreement which had been reached. The court ordered Wal-Mart to pay additional premiums to Transit, in accordance with the manual rates set forth in the policies and with Wal-Mart's actual payroll figures. Wal-Mart appeals each of these determinations.

DISCUSSION

1. *Miro's Authority*

The district court first concluded that Miro's actual atuhority was limited by the terms of the agency agreement in force between Miro and Muldoon (acting in behalf of Transit), which agreement prohibited Miro from entering into agreements utilizing premium rates not on file with appropriate state regulatory authorities.[4] The agreement authorized Miro to issue policies "subject to and in accordance with the insurance laws and regulations of each State, and in accordance with rates, filings, forms, policy limits, underwriting guidelines governing acceptance * * * as directed, filed, and promulgated by [Transit] * * *." Wal-Mart argues that this language amounts merely to

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4. Issues regarding the nature and extent of an agency relationship are, when material facts are undisputed, questions of law reviewable de novo. *Campbell v. Bastian,* 236 Ark. 205, 365 S.W.2d 249, 251 (1963); *Field v. Omaha Standard, Inc.,* 582 F.Supp. 323, 328 (E.D.Pa.1983), *aff'd,* 732 F.2d 145 (3d Cir.), *cert. denied,* 469 U.S. 828, 105 S.Ct. 113, 83 L.Ed.2d 56 (1984) ("If the facts concerning the connection between the parties are not in dispute, questions concerning the existence and the nature of the relationship are properly determined by the court.") *See* 3 C.J.S. *Agency* § 548, at 482 (1973); 3 *Couch on Insurance* 26.61, at 618 (1984). The facts necessary to an analysis of the agency issues presented here were set forth in detail by the district court. Our analysis does not reevaluate these factual determinations, but simply places differing emphasis upon essentially undisputed facts when we believe they are of greater or lessel legal significance.

"instructions" to act lawfully, and that Miro was actually authorized to issue whatever policies he deemed prudent.

We agree with the district court that the language of the agency agreement operated to define the scope of Miro's actual authority. *See* Restatement (Second) of Agency § 33 (1958). The limitations set forth in the agreement imposed substantive boundaries upon Miro's authorized activities. Assuming, as the district court did, that Miro acted unlawfully in entering into the $3.5 million agreement, the district court correctly concluded under the facts presented that Miro acted outside of the bounds of the actual authority granted to him by Transit pursuant to the agency agreement.

With regard to the issue of Miro's apparent authority, however, we disagree with the conclusion reached by the district court. Under Arkansas law, which the parties agree applies to this issue, apparent authority is such authority as "a principal proclaims or permits, such authority which a principal by lack of care causes or allows, or such authority as a reasonably prudent man using diligence and discretion would naturally suppose." *Scholtes v. Signal Delivery Serv., Inc.*, 548 F.Supp. 487, 495 (W.D. Ark.1982). *See Mack v. Scott*, 230 Ark. 510, 323 S.W.2d 929, 931-32 (1959); *Ozark Mut. Life Ass'n v. Dillard*, 169 Ark. 136, 273 S.W. 378, 381 (1925). Two elements must be established to support a showing of apparent authority: "(1) that the principal held the agent out to the public as possessing sufficient authority to embrace the particular act in question, or knowingly permitted him to act as having such authority; and (2) that the person dealing with the agent knew of the facts and acting in good faith had

reason to believe and did believe that the agent possessed the necessary authority." *Central Surety & Ins. Corp. v. O. & S. Wholesale Co.*, 193 Ark. 523, 101 S.W.2d 167, 172 (1937) (quoting 2 C.J. *Agency* § 213, at 574). *See Continental Cas. Co. v. Erion*, 186 Ark. 1122, 57 S.W.2d 1025, 1028 (1933). If an agent acts within the scope of his apparent authority, his acts bind the principal, whether actually authorized or not, and even if contrary to express direction. *See Landmark Savings Bank v. Weaver-Bailey Contractors, Inc.*, 22 Ark.App. 258, 739 S.W.2d 166, 169 (1987).

Transit does not dispute that the first portion of this test, conduct by the principal, is satisfied in this case through Transit's provision of blank policy forms to Miro. The more difficult issue is whether Wal-Mart acted reasonably in believing that Miro possessed sufficient authority to enter into the $3.5 million agreement. We believe it did.

In reaching its conclusion on this issue, the district court focused primarily upon two facts: Wal-Mart's sophistication as an insurance purchaser and the very low premium offered by Miro. The court concluded that the deal offered by Miro was "too good to be true," and that Wal-Mart, as an experienced and knowledgeable insurance buyer, should have known that no reasonable insurer would permit an agent to offer a policy on such terms. There are two flaws in this approach. First, such an analysis places great weight upon events which took place subsequent to the time the contract was agreed upon. The terms offered by Miro appear extraordinarily favorable only because of Wal-Mart's loss experience over the two

years following the initiation of the policy. There was testimony that workers' compensation claims filed by Wal-Mart employees over several years preceding 1982 in the states in which Wal-Mart was self-insured averaged just over $2 million per year. Projected losses for the first policy year were estimated to be under $3 million. Thus, while a $3.5 million guaranteed premium was certainly a competitive offer, it was by no means unreasonably low in comparison to Wal-Mart's demonstrated loss history at the time. The reasonableness of Wal-Mart's actions and perceptions must be judged at the time the contract was entered into, under the facts and circumstances then existing. The district court erred in relying so heavily on Wal-Mart's disastrous loss experience, something about which all the parties were unaware at the relevant point in time.

Additionally, we believe that the district court's analysis improperly imposed upon Wal-Mart an unreasonable level of expertise in state workers' compensation insurance laws and practices. The court found, and we agree, that Wal-Mart was a sophisticated insurance consumer. However, the court also found that such sophistication should have been adequate for Wal-Mart to know without question, before receipt of the actual policy from Transit, that Miro's proposal, in any form, would not have been satisfactory to state insurance regulators. An insured whose principal business is retail sales cannot be reasonably expected to maintain such expertise in the intricacies of state workers' compensation regulatory requirements in each of the many states in which it does business. Under the district court's analysis, Wal-Mart would have been obligated to ascertain, for example, whether its in-

surer had utilized proper rating classifications in each state, whether those classifications had been properly applied to filed rates, and whether the insurer had properly applied filed rate deviations, if any, in each relevant state. Imputing such knowledge, and the investigatory obligations which follow, in an area as complex as workers' compensation regulatory requirements and filings to an insured even as sophisticated as Wal-Mart is not reasonable under the circumstances of this case.

Moreover, the standard applied by the district court imposes an obligation upon Wal-Mart to know when a quoted insurance permium is too low, and to reject it. Such an approach would require an insured to engage in an underwriting analysis of the risk involved to make an educated determination regarding the adequacy of the quoted premium. We believe that the duty to make this determination is better placed upon the insurer, who is undoubtedly in a better position to evaluate the relevant facts. While there may be a point at which a quoted premium is so small in light of previous loss experience that an insured should be charged with knowledge of its inadequacy, we do not believe that this case presents such a scenario.

We find, therefore, that the district court erred in its reliance upon Wal-Mart's purported knowledge of future losses, the requirements of state workers' compensation regulations, and the intricacies of premium underwriting in finding that Wal-Mart acted unreasonably in believing that Miro was within his authority in offering the $3.5 million agreement. Further, the court improperly failed to consider evidence of the circumstances which ex-

isted at the time the agreement was reached. The record reflects that at that time, the insurance industry was extremely competitive. Witnesses referred to the "soft market" for insurance products which was then in existence in which premiums were lowered to obtain preferred clients. Wal-Mart was aware that insurers were willing to reduce premiums to obtain its business.[5] Wal-Mart also knew that there existed numerous mechanisms by which filed workers' compensation rates could be legitimately adjusted to achieve a quoted premium. Devices such as premium discounts, retrospective rating, policy dividends, rate deviations and scheduled rating were available to legally reduce premium charges below what would have to be paid pursuant to filed rates.[6] We believe, at the time Miro approached Wal-Mart with his bid, that Wal-Mart could have reasonably believed that the $3.5 million premium was potentially within the bounds of state requirements. Through hindsight, we now know that the Miro bid was unreasonably low. To require Wal-Mart to have made such a determination in 1982, given the nature of

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5. In addition, many states had, by this time, implemented efforts aimed at deregulating the workers' compensation insurance industry. Minnesota, for example, a state which had required adherence to rates promulgated by a state rating commission, changed its laws in 1979 to require only that workers' compensation insurers not charge more than a maximum rate. *See* Minn.Stat. § 79.21 (1982). Such deregulation efforts added to the growing competitive atmosphere in the industry.

6. For example, there was testimony that in 1984, Transit had filed and received approval in Arkansas for separate 15 and 50 percent deviations from filed rates. Accordingly, the actual premium charged by Transit in 1984 could have been up to 65 percent less than the actual rates filed in Arkansas. The premium which the district court ordered Wal-Mart to pay is based upon filed rates with no discounts or deviations.

the insurance market at the time and the numerous ways in which an insurer might achieve such a rate, is improper. Miro acted within his apparent authority when he offered Wal-Mart the $3.5 million guaranteed premium, and Transit is, therefore, bound by his actions.

2. *Legality of the Agreement*

We must next consider whether the district court correctly found that the premium agreement violates state law. The district court found that there was no need to examine the laws of each individual state in which Wal-Mart did business to make this determination because the agreement violated basic principles of workers' compensation law common to each state's regulatory system. The court found that an agreement to provide workers' compensation coverage for a fixed premium, not to be adjusted for any factor other than a change in payroll, and not tied in any way to rate filings in effect in any state violated the basic statutory concept of workers' compensation, that all employers must provide a specified level of coverage for injured workers at specified and approved rates. The court also found that the agreement was contrary to anti-rebate laws in effect in each relevant state. Wal-Mart argues that both of these conclusions are in error, and that the premium agreement is, or could have been, completely legal and fully enforceable in all states.

After reviewing the record and the workers' compensation laws of the states involved,[7] we agree that the agree-

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7. The states within the coverage of the policies were: Alabama, Arkansas, Florida, Georgia, Illinois, Indiana, Iowa, Kan-

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ment is illegal and violates the law of each state, but for reasons different than those expressed by the district court. First, while it is true, as Wal-Mart contends, that there has been a marked trend away from strict regulation of the rates which workers' compensation insurers must charge, all states, including those in which insurers are free to charge whatever rates they desire (the so-called "open-rated" states), require that insurers file their rating schedules and policy forms for review by state authorities, who may reject rate proposals which would result in inadequate, excessive or discriminatory charges.[8] In addition, each state prohibits any person or organization from knowingly submitting false or misleading information to the regulatory authorities responsible for such review.[9]. Regardless of the degree of control and super-

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sas, Kentucky, Louisiana, Mississippi, Missouri, Nebraska, North Carolina, Oklahoma, South Carolina, Tennessee, and Texas. New Mexico was listed on the first policy, but not on the renewal policy.

8. Ala.Code § 25-5-8(f)(2) (1986); Ark.Stat.Ann. § 23-67-119(1)(A) (1987); Fla.Stat.Ann. § 627.091(1) (West 1984); Ga.Code Ann. 33-9-2(a) (1987); Ill.Stat.Ann. ch. 73 ¶ 1065.4(1) (Smith-Hurd 1988); Ind.Code Ann. § 27-7-2-13(a) (1986); Iowa Code Ann. § 515.4(1) (West 1988); Kan.Stat.Ann. § 40-928 (1986); Ky.Rev.Stat.Ann. 304.13-051 (Baldwin 1987); La.Rev.Stat.Ann. § 22:1407(A)(1) (1973); Mo.Rev.Stat. § 379.321(1) (1986); Neb. Rev.Stat. § 44-1405 (Reissue 1984); N.M.Stat.Ann. § 59A-17-10 (1984); N.C.Gen.Stat. § 58-124.20 (1982); Okla.Stat.Ann. tit. 36 903 (West Supp.1988); S.C. Code Ann. § 38-43-340 (Law. Co-op. 1985); Tenn.Code Ann. § 56-5-306(b) (Supp.1987); Tex. Ins.Code Ann. § 5.15(a) (Vernon 1981).

9. Ala.Code § 27-13-77 (1986); Fla.Stat.Ann. 627.361 (West 1986); Ga.Code Ann. § 33-9-35 (1987); Ill.Stat.Ann. ch. 73 ¶ 1065.14 (Smith-Hurd 1988); Ind.Code Ann. § 27-1-22-17

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vision each state exercises over the specific rates workers' compensation insurers may charge, all require that these informational filings be made. We believe that the arrangement in effect in this case stands in clear violation of this statutory requirement.

There is no dispute that the manner in which the policies issued to Wal-Mart reached the agreed upon premium was by manipulation of payroll amounts. The payrolls for each state were depressed below what was actually anticipated in order to reach the $3.5 million total, with no intent by either party to adjust the payroll figures to reflect actual amounts at a later time. The district court found, and we agree, that all parties, at some time during the policy period, knew that the payroll figures had been depressed, should have taken action to resolve the misrepresentations, but did nothing. As written by Miro, the policies did not embody the parties' actual agreement, which was to provide coverage for the full employee payroll for $3.5 million. As written, therefore, the policies operated to deceive state regulatory authorities, because, in actuality, they embody a rating schedule which

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(1986); Iowa Code Ann. § 515A.14 (West 1988); Kan.Stat.Ann. § 40-938 (1986); La.Rev.Stat. Ann. 22:1416 (West Supp.1988); Miss.Code Ann. § 83-3-119 (1973); Mo.Rev.Stat. § 379.353 (1986); Neb.Rev.Stat. § 44-1436 (Reissue 1984); N.M.Stat.Ann. § 59A-17-31 (1984); Okla.Stat.Ann. tit. 36 § 935 (West. Supp. 1988); S.C.Code Ann. § 38-43-100 (Law. Co-op. 1985); Tex. Ins.Code Ann. § 5.21 (Vernon 1981). Arkansas, Kentucky, North Carolina and Tennessee had no comparable statute during the revelant time period. However, each state's general prohibitions against misrepresentation and fraud upon state officials would undoubtedly extend to the conduct at issue here.

the parties never planned to file with any state. It would be impossible for state regulators to test the policies to ascertain whether the rates charged were inadequate, excessive or discriminatory, because the policies on their face did not reveal the true rates being charged. While the policies theoretically could have been structured to meet the $3.5 million bottom line through the use of legitimate discounting procedures, such legitimate procedures were not utilized here. The policies materially misrepresented information required by law to be reported truthfully in every state. They were deceptive as written, and thus violate the laws of each state involved.

3. *Effect of Illegality*

The district court found that the insurance policies were enforceable pursuant to the terms appearing on their face, computed according to Wal-Mart's actual payroll. Accordingly, the court ordered Wal-Mart to pay Transit additional premiums in an amount equal to what would have been due under the policy had actual payroll figures been utilized. The court said that whether the agreement regarding premium was illegal or not, workers' compensation law requires that the coverage terms of the policies be enforced as written.

We find such a result inappropriate given our conclusion that the agreement is illegal in its entirety. In its analysis, the district court separated the insurance agreement into two parts, a premium portion and a coverage portion, and enforced one segment but not the other. In reality, there was but one contract in effect between Transit and Wal-Mart, renewed after the first year, which con-

tract consisted of premium and coverage terms, both of which were essential to a complete and binding agreement. *See, e.g., Tanna v. Johnson,* 233 Ark. 409, 344 S.W. 2d 846, 851(1961) (enforceable contract requires meeting of the minds as to all material terms). As clearly found by the district court, Transit agreed to provide workers' compensation benefits to Wal-Mart employees for a premium of $3.5 million. If the premium terms of the contract is illegal and unenforceable, as we believe it is, the coverage portion of the same contract is necessarily unenforceable as well. The district court's resolution of this matter requires the execution of contractual terms to which there was no agreement by any party to the negotiations. Such a resolution is inappropriate under these circumstances. *See Borden, Inc. v. Smith,* 252 Ark. 295, 478 S.W.2d 744, 747 (1972) (court should not vary the terms of an agreement between the parties; to do so would "mean that we were making a new contract and we have consistently held that this will not be done.").

We find that a more fitting resolution to this dispute is to apply the doctrine of in pari delicto, and leave the parties as they presently stand. Arkansas has recognized and applied the doctrine of in pari delicto when parties to an illegal contract are equally culpable. "The general rule with respect to illegal contracts is that neither courts of law nor of equity will interpose to grant relief to the parties, if they have been equally cognizant of the illegality." *City Nat'l Bank v. First Nat'l Bank and Trust Co.,* 22 Ark.App. 5, 732 S.W.2d 489, 495-96 (1987). *See Long v. Mabry,* 250 Ark. 947, 470 S.W.2d 319, 321 (1971) (where parties to illegal bargains are in pari delicto, the law will

"leave them where it finds them."). *Womack v. Maner,* 277 Ark. 786, 301 S.W.2d 438, 439 (1957). If the court finds that the parties are equally at fault in perpetrating the illegal transaction, relief will be unavailable to either party to the transaction. *Id. See also Williams v. Wilson,* 181 F.Supp. 351, 354 (E.D.Ark. 1960). As noted by the district court, the principal purpose of the rule is to discourage the making of illegal agreements. *See generally* 17 Am.Jur.2d *Contracts* § 216, at 585-86 (1964) ("The rationale of the rule rests upon the broad ground that no court will allow itself to be used where its judgment will consummate an act forbidden by law, and upon the policy of discouraging illegal and corrupt agreements by refusing all judicial aid to the parties thereto."). The rule applies with equal force where the contract has been executed in whole or in part. *Id* at § 223.

The level of culpability of the parties was best put, we think, by the district court when it said, "there is more than enough fault to go around in this case." *Wal-Mart,* 664 F.Supp. at 1269. The district court's opinion explains in detail the various activities of Transit, through its agent Miro, and of Wal-Mart, by which each was or became an active participant in carrying out the illegal portions of the insurance contract. Transit is charged with responsibility for the acts of its agent, Miro, who structured the deal from the start. Wal-Mart, as the district court found, became aware of the depressed premium figures, and did nothing. Though Wal-Mart acted reasonably in its belief at the outset that Miro could have lawfully structured the policies to reach the quoted premium, when the policies were later delivered and Wal-Mart became aware of the manner in which the quoted premium

was actually achieved, the reduction of payroll, Wal-Mart should have taken corrective action. It is at this point, when Wal-Mart saw how Miro structured the policies, that Wal-Mart became chargeable with the illegality.[10] We believe the district court correctly concluded that all parties were active and willing participants in a knowingly illegal venture.[11]

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10. The district court also placed great weight upon an incident which we agree demonstrates Wal-Mart's cognizance of and willingness to participate in the illegal arrangement after delivery of the policies. In late 1984, Miro told Wal-Mart and A & A that a transfer of $6 million needed to be made to "satisfy statutory requirements." Miro acknowledged, according to their agreement, that Wal-Mart did not owe additional premiums, but suggested that Wal-Mart transfer the money to Miro, who would transfer it to his offshore captive reinsurance company, who would then transfer it back to Wal-Mart as a dividend. Wal-Mart, without inquiring about the specific regulatory requirements which were involved or questioning why such a sham payment had to be made, agreed to the transfer with assurances that the funds would be returned. We agree with the district court that Wal-Mart's willingness to participate in this transaction, though it was never consummated, speaks loudly about its knowledge of the propriety of the entire arrangement. For a more detailed description of the proposed transaction, see *Wal-Mart*, 665 F.Supp. at 1250-51 & 1260-61.

11. An additional issue raised by the parties, but not considered by the district court, involves whether Transit's receiver is bound by the illegal acts of the insolvent prior to receivership. Transit relies upon a line of cases following *D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 315 U.S. 447, 62 S.Ct. 676, 86 L.Ed. 956 (1942), in which the Supreme Court held that the FDIC is not bound by undisclosed arrangements affecting the genuineness or integrity of notes in the insolvent bank's portfolio. Transit asks that we apply a similar doctrine to it as the receiver of an insolvent insurer. Transit cites no cases extending the *D'Oench* doctrine beyond the confines of the banking industry, and we are not persuaded to take such a step here.

Accordingly, we find that the district court should have found the parties in pari delicto and refused to grant relief of any sort. The district court discussed the issue, but found that application of the doctrine was inappropriate because Wal-Mart would supposedly receive the full benefit of its illegal activities, thereby encouraging rather than deterring the formation of illegal bargains. We disagree. The district court's analysis places undue emphasis on the fact that the agreement has been partially executed, a fact which, as noted, is not pertinent to the application of the in pari delicto doctrine. In any event, we believe, to the contrary, that application of the doctrine here would work to discourage insurers from permitting agents to quote premiums and structure policies in violation of state insurance regulations. Requiring the payment of greater premiums by Wal-Mart not only stands in direct conflict with the terms of the original agreement as all parties expected it to be carried out, but operates to reward Transit for structuring an illegal arrangement which it, as the insurer, was in the best position to prevent. The district court should have denied relief on both Wal-Mart's action for a declaratory judgment and Transit's counterclaim for payment of premiums.

One further comment on the practical effect of such a resolution of this case is necessary. As noted, while Transit has paid somewhere between $16 and $21 million in claims on the two workers' compensation polities, the parties expect that a significant amount of claims are yet to be filed and paid. The ultimate responsibility for payment of these claims, in the absence of valid workers' compensation insurance coverage, rests with Wal-Mart as the employer. *See New Hampshire Ins. Co. v. Logan,* 13 Ark.

App. 116, 680 S.W.2d 720, 722 (1984) ("[T]he primary liability for workers' compensation is upon the employer and * * * insurance coverage does not relieve the employer of that liability."); *McGehee Hatchery Co. v. Gunter*, 234 Ark. 113, 350 S.W.2d 608, 611 (1961). As a leading commentator explained:

> While as between the insurer and employer, the former is liable to pay such awards, and the employer may recover back from the insurer payments he has made, nevertheless the employer is primarily liable and on failure of the company to pay any award, the employer will be obligated therefor. Thus, if the insurer becomes insolvent, the employer must discharge any award made, or any other sums due the employee.

7B Appleman, *Insurance Law and Practice* § 4624, at 213-14 (1979). Thus, assuming that Transit does not pay further claims, either because of insolvency or because the insurance agreement is unenforceable against it, the responsibility for payment of these claims rests with Wal-Mart.[12] We simply note that under our resolution of this case, there is no risk that injured employees will be left uncompensated.

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12. One other potential source of funds to pay claims made by Wal-Mart employees is state insurance guaranty funds, established to assist in payment of claims against insolvent insurers. However, such funds, in general, apply only to "covered claims," a term generally defined to include only those claims within the coverage of a valid policy of insurance in effect at the time of the insolvency. 19A Appleman, *Insurance Law and Practice* § 10801, at 367-68 (1982). *See*, e.g., Fla.Stat.Ann. § 631.54(3) (1984); Ill.Stat.Ann. ch. 73 ¶ 1065.84-3 (Smith-Hurd Supp. 1988); Mo.Rev.Stat. § 375.785 (3)(2) (1986); Neb.Rev.Stat. § 44-2406 (Reissue 1984); N.C. Gen.Stat. § 58-155.45(4) (Supp.1987).

CONCLUSION

The district court placed the primary responsibility for compliance with state workers' compensation laws upon the insured, Wal-Mart. Given all the circumstances of this case, we believe this obligation more appropriately rests with the insurer, Transit. We reverse the decision of the district court with respect to Transit's counterclaim, and remand with direction to dismiss the case without relief to any party.[13]

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13. Given our resolution of the claims between Wal-Mart and Transit, we need not consider the district court's resolution of Wal-Mart's third-party action against A & A. It, of course, shall be dismissed along with the other claims in the lawsuit.

WAL-MART STORES, INC., Plaintiff

v.

Lewis R. CRIST, Receiver for Transit Casualty Company in Receivership,

Defendant.

WAL-MART STORES, INC.,
Third-Party Plaintiff on

Counterclaim,

v.

ALEXANDER & ALEXANDER, INC.,
Third-Party Defendant on

Counterclaim.

Civ. No. 85-5036.

United States District Court,
W.D. Arkansas,
Fayetteville Division.

July 6, 1987.

Insured under workers' compensation policy filed declaratory judgment action against insolvent insurer, seeking to enforce provisions of alleged side agreement for provision of coverage for flat and guaranteed premium. Insurer counterclaimed for additional premiums allegedly due, and insured brought in insurance brokerage firm acting as its consultant as third-party defendant. The District Court, H. Franklin Waters, Chief Judge, held that: (1) evidence of side agreement was admissible but insurer's agent was without actual or apparent authority to enter into that agreement, which even insured's experts admitted would not have been approved in Arkansas or any other state; (2) insured would be required to pay prem-

iums specified in policy, with prejudgment interest to be determined by insurer's receiver, and side agreement was unenforceable and void; (3) tail coverage under policy was properly issued within agent's authority; and (4) consultant was not liable for difference between premiums that insured would be required to pay and those which insurer's agent originally agreed to accept.

Ordered accordingly.

Stuart Cotton, Rein, Mound & Cotton, New York City, Robert Robinson, Hatfield, Robinson, Hodges, Marshall, Jordan & Shively, Little Rock, Ark., and Robert R. Rhoads, Asst. General Counsel, Bentonville, Ark., for Wal-Mart Stores, Inc.

W. H. Sutton and C. Tab Turner, Friday, Eldredge & Clark, Little Rock, Ark., for Lewis R. Crist.

Philip J. Walsh, Wilson, Elser, Edelman & Dicker, New York City, and Patrick J. Goss, Wright, Lindsay & Jennings, Little Rock, Ark., for Alexander & Alexander, Inc.

MEMORANDUM OPINION

H. FRANKLIN WATERS, Chief Judge.

I. The Litigation

This is exceptionally complex litigation between Wal-Mart Stores, Inc., one of the largest retail concerns in the country, and the Receiver of an insolvent insurance carrier, Transit Casualty Company, which wrote workers'

compensation insurance covering Wal-Mart's employees in eighteen states in which Wal-Mart then had facilities.

The litigation started as a declaratory judgment action filed by Wal-Mart against Transit (prior to it being declared insolvent) seeking to enforce the provisions of an agreement that it says it entered into with Transit through one of Transit's agents, calling for Transit to provide workers' compensation coverage in those states for two separate policy periods, one commencing February 1, 1983, and ending January 31, 1984, and the second beginning February 1, 1984, and ending January 31, 1985. It is alledged that this agreemet called for Wal-Mart to pay premiums not to exceed $3,500,000 for each policy year for such coverage.

Transit answered, substantially denying the allegations of the complaint, and alleging that the agreement which Wal-Mart seeks to enforce in this litigation is contrary to law and, thus unenforceable. It counterclaimed, seeking to recover, in addition to the $7,000,000 in premiums already paid by Wal-Mart for the coverage, additional premiums approximating $20,000,000.

In its reply to the counterclaim, Wal-Mart denied its allegations, and affirmatively pled that, in the event the agreement referred to is contrary to law, then Transit is barred from recovery on its counterclaim because it is *in pari delicto*. Subsequently, Wal-Mart amended its complaint to include allegations in relation to certain retroactive coverage that it says it contracted for which it claims Transit had, since the original complaint was filed, ceased performing the obligations required by such coverage. In addition, Wal-Mart brought into the lawsuit,

as a third-party defendant, Alexander & Alexander, Inc., (A & A) an insurance brokerage firm which it claims provided consulting services during the period relevant to this litigation. It seeks recovery from A & A of any amounts that it is required to pay to Wal-Mart.

Approximately sixteen months aftter the original complaint was filed, and after numerous amended pleadings and various motions were filed and disposed of, the Circuit Court of Cole County, Missouri, acting on a petition for liquidation of Transit filed by the Acting Director of the Division of Insurance, Department of Economic Development, State of Missouri, found Transit to be insolvent and appointed a Receiver for it. After a short stay of all litigation, this matter was allowed to proceed with Transit's interests being pursued by the Receiver, Lewis R. Crist, who was also at the time Director, Division of Insurance, Department of Economic Development, State of Missouri.

After substantial additional pretrial motions, including a motion for partial summary judgment, were filed and disposed of by the court, the matter was tried. Initially, a jury was selected at the request of one or more of the parties, and the case was tried to that jury for a period of approximately four and one-half days. At that time, all parties advised the court that they would waive a jury and would agree to have the matter tried and decided by the court. Whereupon, the jury was excused, and testimony was completed in two and one-half additional trial days.

The matter was taken under advisement so that the attorneys for the parties could file briefs in relation to the issues. The attorneys for the parties, all of whom per-

formed admirably during the trial of this complex litigation, also favored the court with excellent post-trial briefs. In addition an *amicus curiae* brief was filed in behalf of the Director of the Missouri Division of Insurance and was joined in and adopted by the State of Texas acting through its Attorney General. The court has considered the briefs, and after a careful consideration of the evidence received at the trial, is prepared to rule.

II. The Facts

Transit Casualty Company was, at least when compared to other insurance carriers, a relatively small insurance carrier which, during the 1960s and 1970s, specialized in transportation related insurance, insuring primarily truck and bus operations. Howexer, it had authority to write most types of insurance in most of the states.

By the late 1970s, because of changes in the transportation industry and increased competition from other carriers, Transit was "watch[ing] [itself] go out of business," according to Robert J. Olson, an officer with the company at the time. In approximately 1981 Transit's management decided to "get into the captive movement" and use captive insurance companies to reinsure Transit policies. In this manner, Transit hoped and intended to write insurance policies in lines of business in which it had not previously been involved and in which its employees had little if any experience. The officers of the company decided to proceed into those areas in that manner because, according to Olson, the idea was "that you don't have an insurance risk, you have a credit risk."

Because Transit had litttle if any experience in this area of insurance, its management decided that it needed

to create a relationship with someone or some entity that did. Negotiations began with Donald F. Muldoon who had prior experience with the types of insurance that would be involved, particularly in "captive programs." These discussions resulted in the formation of a company known as Donald F. Muldoon & Co., Inc. (Muldoon), which was established in 1981 to "do fronting" for Transit. Transit retained a 24% ownership interest in Muldoon.

In January of 1982 Transit and Muldoon entered into a "Managing Agency Agreement" which substantially gave Muldoon the authority to issue any Transit policy which Transit was authorized to issue in any state in which it was qualified to issue insurance policies. The agreement contained certain limitations which do not appear to be material to the issues in this case, except that the agreement provides that Muldoon had the authority to issue coverages on behalf of the company using "policies, contracts, certificates, utilizing rates and forms, endorsements and binders on behalf of the company which had been approved by the company and which have been approved by and/or conform with any applicable state insurance department laws and regulations." The agreement provided that Muldoon would "observe and comply with all insurance laws, rules and regulations of all states and the District of Columbia wherein any business is transacted for and on behalf of the company."

The Managing Agency Agreement authorized Muldoon to request, from time to time, that certain sub-agents be appointed with substantially the same authority as Muldoon in relation to the production and issuance of Transit insurance policies. Shortly after Muldoon was appointed

Transit's managing agent, a former Alexander & Alexander, Inc., employee introduced Donald F. Muldoon to Carlos Miro, himself a former A & A employee. Mr. Muldoon recommended Miro, then doing business as Miro & Associates Risk Management, Inc. (Miro), to become a sub-agent of Transit. Miro was appointed a sub-agent and a "Managing Agency Agreement" (Wal-Mart Ex. 19) was entered into between Donald F. Muldoon & Co., Inc., and Miro & Associates, Inc. The agreement authorized Miro to

> solicit and bind only the types and lines of business as hereafter stated. under the terms and conditions of this agreement, subject to and in accordance with the insurance laws and regulations of each state, and in accordance with rates, filings, forms, policy limits, underwriting guidelines governing acceptance of such business, and procedures, all as directed, filed and promulgated by the company from time to time; and to issue policies and certificates of such insurance on forms provided by the company, utilizing rates filed by the company pertaining to such coverages; and to amend such policies by endorsements authorized by the company; and to cancel such policies.

Muldoon provided Miro with blank policy forms to issue on Transit's behalf, and all of Miro's business was to be written or fronted on Transit policies and reinsured with Miro's captive reinsurers. For providing its insurance policies, name, filings, and, in effect, guaranty, Transit was to receive a fronting fee of 9% of the premium paid.

Under the agency agreement, Transit had the right to audit its agent's records and it recognized that there was a danger that the agent would exceed its authority.

Accordingly, Transit had the right to cancel coverages if an audit revealed that an agent had exceeded its authority.

After Muldoon's appointment as Transit's managing agent, and Miro's appointment as a sub-agent, the Transit captive program grew very fast. According to Olson, in 1981 premiums from the program went from "zero to $40,000,000; and in 1982 it exceeded $100,000,000." By 1983, Miro was Muldoon's biggest premium producer. All of the policies issued by Miro on Transit paper were to be 100% reinsured. If the program had functioned as designed, there was minimal retained risk for Transit so long as reinsurance remained in place with solvent reinsurers.

Wal-Mart Stores, Inc., one of the largest retailers in the country, is headquartered in Bentonville, Arkansas. During 1980-1981 Wal-Mart was self-insured for its workers' compensation and general liability risks in all states in which it did business except the state of Texas and three or four southern states in which it had a limited number of employees. During that period of time it paid a monthly fee of $6,000 (later reduced to $3,000) to Alexander & Alexander, Inc., to act as its insurance consultant.

In April, 1980, John Sooter, an accounting graduate from the University of Arkansas in 1970, was appointed Wal-Mart's Director of Risk Management. Prior to that time, he had been an internal auditor for Wal-Mart and before joining Wal-Mart was an internal auditor for Standard Oil of Indiana (later Amoco Production Company) and Pan-American Petroleum Corporation of Tulsa, Oklahoma. While Sooter, probably understandably, attempted to denigrate his ability and experience as a Risk Manager,

the court believes that, at the time of his appointment to the Risk Management job, he was a sophisticated businessman and accountant. In addition, the court finds that he practically had at his beck and call, for $6,000 per month, the substantial insurance experience present within Alexander & Alexander. The evidence indicates that the individual from Alexander & Alexander who primarily consulted with him was George Hallinan, Vice President, a person with in depth experience in almost all phases of the insurance business for approximately thirty years.

In late 1982, Sooter asked Hallinan to obtain quotes for the Texas workers' compensation coverage which was up for renewal or replacement in a few months. In November of 1982, Hallinan brought to Sooter two quotes for the Texas coverage. One was from the Hartford Insurance Company and one was from Transit through Miro. Sooter was certainly sophisticated enough to recognize a "good deal" when he saw one. When he saw the quote on the Texas workers' compensation coverage, he immediately asked Hallinan to determine if Miro would be interested in bidding on the workers' compensation coverage for all states, replacing the self-insurance which Wal-Mart had in the other states. After being contacted by Hallinan, Miro indicated that he would gladly provide such quotes.

While it is not apparent from the evidence that Miro used much of the information to make the quote that he made, it appears from the evidence that he at least had access to Wal-Mart's payroll figures for the previous five years and also loss history for the self-insured states. This loss history was provided by a subsidiary of Alexander & Alexander, Alexsis, which had provided the ad-

justing services for Wal-Mart during the period that its workers' compensation coverage was self-insured.

In mid-January of 1982, Sooter, Hallinan and Pete Proffer, of Alexsis' St. Louis office where Wal-Mart's self-insured claims files were kept, attended a meeting in Miro's Dallas office. The meeting was also attended by two of Miro's employees who had also previously been employees of A & A.

It was obvious that Miro was the decision maker in the group. Certain testimony in relation to Miro is illuminating. When Sooter was asked if Miro was a "young man," he replied: "He appears to be a very young man. I don't believe he is quite as young as you would think he was if you saw him." Then later in his testimony he said: "He was just confident. He felt like he was intelligent and everybody around him thought he was intelligent and he was a very good speaker and just displayed a good bit of confidence." When he was asked if it was fair to say that he was "a pretty slick guy," he said, "I'd say he was pretty slick, yes. . . . Towards the end he had developed quite a staff and I don't know a number, but they started out with one little corner in an office building and they ended up with at least half of the floor of an office building."

At this Dallas meeting, and a subsequent one, Miro presented to Wal-Mart a quote which is set forth in Plaintiff's Exhibit 1. The court believes that the evidence shows, without question, that Miro proposed to write all of Wal-Mart workers' compensation coverage in all of the states where it did business for a flat and guaranteed premium of $3,500,000. This premium, the court believes the

evidence clearly shows, was not to be affected in any way by any factors other than an increase or decrease in Wal-Mart's payroll from the estimated figure of $547,000,000. The court believes that the evidence indicates that no one at either meeting, probably including Miro, really understood anything Miro said about how the $3.5 million premium was calculated, or the figures in Plaintiff's Exhibit 1, except for the bottom line figure. Everyone knew that he was bidding $3.5 million to provide the coverage, and that appears to be all that Sooter of Wal-Mart and his consultant, Hallinan, were interested in. The testimony indicates that, apparently after arriving at the $3.5 million figure, Miro did some calculation on a Casio calculator and arrived at a "composite rate" of .63985 per $100 of payroll, determined simply by dividing $3,500,000 by $547,000,000 and multiplying the quotient by 100. The court believes that the evidence indicates that the premium of $3.5 million was "pulled out of the air" and that the composite rate was a mere mathematical calculation which could have been made by anyone with a calculator and rudimentary knowledge about how to use it. The evidence does not indicate that the other figures and calculations shown in Plaintiff's Exhibit 1 had anything to do with the rate to be charged and the premium to be paid by Wal-Mart for this substantial insurance coverage. At least, no witness was able to explain to the court any other method for calculating the composite rate, and Plaintiff's Exhibit 1 appeared to be largely meaningless to the witnesses who testified, and is certainly meaningless to the court, even after several days of testimony. Unfortunately, Mr. Miro was no longer in the United States at the time of the trial, and did not testify.

During the Dallas meeting, either Miro was asked if he would be interested in bidding on what became known as the "tail coverage" or he volunteered to do so. In any event, Miro was asked to also cover, through Transit insurance policies, Wal-Mart's liability for workers' compensation benefits for the period from February 1, 1980, to January 31, 1983, when Wal-Mart was self-insured. In other words, Miro was asked to cover for a period of three years any Wal-Mart liability for workers' compensation benefits, whether they were known or unknown. In addition, he was asked to provide general liability coverage covering claims resulting from incidents which occurred from February 2, 1980, to October 15, 1981, again, whether they were known or unknown.

Miro agreed to provide this "tail coverage" for $2,852,000, the aggregate amount of "reserves" which Alexsis had established on incurred and reported claims (known claims). Apparently nothing was charged for incurred but not reported (unknown) claims. Miro said he could do that because he would invest the premiums in "Euro dollars." Although Alexsis, through Proffer, offered to make the claims files available, Miro indicated that he had worked with Alexsis during his tenure with A & A and that he was "familiar with Alexsis and had no problem with their reserves."

In short, the court is convinced that the evidence shows, whether right or wrong, that Miro, in behalf of Transit, agreed to provide workers' compensation insurance coverage for Wal-Mart's employees in all states for a guaranteed premium of $3,500,000, to be affected by absolutely nothing except increases or decreases in Wal-

Mart's payroll. In the event of an increase or decrease, the premium would be adjusted using the "composite rate" of .63985, the figure calculated on his Casio. In addition, the "tail coverage" would be supplied for a guaranteed premium of $2,852,000, irrespective of what the losses turned out to be (and as will be indicated below, they turned out to be disastrous).

During the second meeting, Miro signed a binder using the figures in his proposal, gave it to Sooter, and they shook hands on the "deal." Thus, the court is convinced that the evidence indicates that Miro agreed to provide, and Wal-Mart quickly agreed to accept, a "deal" in which both the workers' compensation coverage and the tail coverage would be provided for a guaranteed premium of $6,352,000. It appears to the court that loss experience played little if any part in development of the premium, and the "deal" was that it would play no part in what Wal-Mart ultimately paid for its coverage. In other words, if its loss history was substantially greater than that of others in the industry (which turned out to be the case), Wal-Mart still would pay no more than the agreed amount for its coverage.

After the meeting in which the "deal" was made, Miro prepared and forwarded to A & A, Wal-Mart's consultant, the insurance policies received as Plaintiff's Exhibits 2 and 3. The workers' compensation policy (Plaintiff's Ex. 2) was issued to Wal-Mart by Miro utilizing Transit policy forms on file with the appropriate state regulatory body. The policy contained a detailed provision for the computation of premiums based on state rates from National Council of Compensation Insurers (NCCI)

manuals on file. This policy listed the sixteen states in which Wal-Mart at the time did business and purported to break Wal-Mart's payroll down into the various job classifications provided for in the NCCI manual on file with most states. The NCCI rate was applied to the purported payroll by classification, and a total premium of $3,967,064 was calculated. Not surprisingly, sufficient discounts were applied on the declarations page to reduce the premium to exactly $3,500,000, the amount earlier agreed to. This workers' compensation policy also covered the tail coverage in relation to compensation benefits. In addition, the general liability policy (Plaintiff's Ex. 3) was prepared and issued providing the retroactive general liability coverage which Miro had agreed to provide.

These policies, after having been forwarded to A & A, were accepted by them and forwarded to Sooter at Wal-Mart. Sooter reviewed them and placed them in the book where he kept all policies.

As indicated above, the workers' compensation policy appears, on its face, to be a standard policy using manual rates, and appears regular on its face. In fact, the policy when issued contained an endorsement, signed by Paul Stanley, an officer for A & A, Wal-Mart's consultant, which provided that: "It is agreed that the premium for the policy is subject to an experience modifier not available at the time of policy issuance. Such experience modification, when determined, if different from the modification shown on the policy, will be stated in an endorsement issued to form a part of the policy." It should be noted that even though Sooter and officials of A & A contend that this was not part of the "deal" (and the court

believes that it was not), this endorsement was signed by an officer of A & A and included in the policy which was subsequently forwarded to Sooter at Wal-Mart.

Sometime after the policy arrived, Sooter or one of his employees noted that, when the payroll figures shown in the policy and purportedly used to calculate the premium were added, the total was considerably less than the estimated payroll of $547,000,000. (The court believes the total of these figures is slightly in excess of $249,000,000.) When this was noted, Sooter contacted Hallinan at A & A and was told that "there was no problem." Hallinan told Sooter not to be concerned because it was "a really common practice" to depress payrolls to come up with an agreed upon premium. One of Miro's employees later confirmed that Miro had "backed into" the premium by depressing the payroll. In other words, it appears to the court that Hallinan knew at the time that what Miro had actually done was arrive at the bottom line and then plug into the formula provided for in the policy whatever figures were necessary to arrive at the bottom line. It is also obvious that Hallinan accepted this as being a "common practice" and told Sooter that there was nothing wrong with it. The policy as written was accepted by Sooter upon the recommendation of Hallinan, his $6,000 per month consultant.

As indicated, in contracting to provide the tail coverage Miro had "purchased" the Wal-Mart reserves and had covered all of Wal-Mart's liability for the prescribed time, whether known or unknown, for the total of the reserves that had been set up by the adjuster. As indicated, this proved to be disastrous. Approximately 185 new claims

were reported to Wal-Mart after the "purchase" and Alexsis created approximately $666,000 in additional reserves for these new claims. In addition, there were adverse developments on several major cases including one in which a Wal-Mart customer had been hit above the eye while using an exercise machine in a Wal-Mart store. Alexsis had reserved that incident at $750 and Miro had "bought it" for that. It later resulted in a judgment of $135,000. A subrogation suit later recovered $88,000 which was paid into the registry of the court pending the outcome of this case.

Another case involved a "slip and fall" in front of a Wal-Mart store. It was initially reserved for $4,000, and was accepted by Miro at that figure, but later resulted in a $200,000 verdict.

When things began to "go bad" in relation to the tail coverage, Muldoon in behalf of Transit had an independent adjuster, Wendell Donahue, review the Alexsis files. He found many files in which a zero reserve was shown. He inspected 170 claims in which the reserve was over $5,000, and found that 103 of them were severely under reserved.

In late August of 1983, Sooter, Hallinan, Miro and one of Miro's employees met in Bentonville to discuss the possibility of providing Wal-Mart with a Transit general liability policy efefctive October 1, 1983. Miro was very interested and sent a written proposal offering general liability coverage. He also offered, as part of the package, to renew the workers' compensation coverage for a maximum premium of $3,500,000. Hallinan sent a letter to Sooter confirming Miro's renewal proposal for " the same guaranteed maximum premium." There were to be no

other adjustments to this figure. Hallinan later confirmed in an October 14, 1983, letter to Miro Wal-Mart's "firm order" to renew the workers' compensation policy on the "same terms, conditions and premium as the current policy." In December of 1983, Sooter, Proffer and Hallinan met with Carlos Miro and some of his employees in Miro's Dallas office and Miro confirmed the renewal. Sooter was asked to prepare an estimated payroll for the renewal period. He first provided an estimate of $551,000,000, which he later revised to $630,000,000.

In January of 1984, Robin Page, one of Miro's employees, wrote to Hallinan suggesting that the workers' compensation premium for the second policy be increased to a little more than $4,000,000 for the coming year to reflect the increased payroll. Page wanted to apply the same "composite rate" of .6398 calculated by Miro at one of the early meetings as outlined above. When that "composite rate" was applied to the estimated payroll of $630,000,000, it resulted in a premium of $4,031,623.

Hallinan and Sooter discussed the proposal. They believed that Miro had already agreed to the same maximum premium, $3,500,000. This led to a June 12, 1984, meeting in Kansas City. Page, Hallinan and Sooter attended. By this time, Wal-Mart had calculated its actual 1983-84 payroll and reported a figure lower than the $547,000,000 estimate. This would result in a return premium to Wal-Mart of slightly in excess of $362,000. It turned out that Sooter's estimate of the 1983-84 payroll was much too low, but that was not discovered until several months later. In any event, based on what he apparently believed to be the lower total payroll, Sooter

agreed to forego the return premium which he believed was due Wal-Mart if Miro would agree that the index figure or "composite rate" for the workers' compensation renewal be lowered to provide for a $3,500,000 maximum premium based on the $630,000,000 estimated payroll. The new "composite rate" would be .55555 per $100 of payroll which, not surprisingly, is the result when $3,500,000 is divided by $630,000,000 and the quotient multiplied by 100. Again, it was that simple. Miro and Wal-Mart negotiated a guaranteed premium and the "composite rate" was changed as necessary to reflect it. The rate had nothing to do with Wal-Mart's loss experience which, by that time, everyone involved knew, or should have known, had been dismal. Miro prepared and forwarded to Hallinan the renewal policy (Plaintiff's Ex. 9) and Hallinan delivered it to Sooter. Again, it appears to be a standard workers' compensation policy listing the states in which Wal-Mart had employees, and reflecting standard NCCI rates. The purported payroll was broken down into job classification categories, and the rate for those categories applied. The premium purportedly developed through this method was reduced by sufficient discounts to arrive at the agreed $3,500,000 premium. Again, the policy called for an experience modifier endorsement to be attached. Although Sooter says that he did not add the payroll figures shown, it is clear, that by this time, everyone concerned knew that those figures meant nothing other than they were the figures necessary to "back into" the agreed premium. In fact, the total of the payroll figures used in the policy appears to be $263,788,776 on a payroll that was estimated by Wal-Mart to total for the policy year $630,000,000. This policy was forwarded by Hallinan, with its obvious

deficiencies and misstatements, to Sooter, apparently because Hallinan believes, according to his testimony, that such misstatements and untruths are common practice in the insurance industry. The policy was accepted by Hallinan and Sooter.

In July of 1984, shortly after the second policy was issued, Hallinan's assistant sent Sooter endorsements No. 9, 10, 11 and 12 for the second year policy, and endorsement No. 16 for the first year policy. Endorsements No. 9 and No. 16 contained experience modifiers prepared by NCCI showing how Wal-Mart's loss experience compared with like employers in similar industries. The endorsement for the first year policy showed an experience modifier of 1.70, and for the second year, 1.73. This means that, according to NCCI, Wal-Mart's loss experience was 70% and 73% greater than the industry average. This means, if the provisions of the policies are complied with, that the premium would have to be adjusted upward 70% for the first policy, and 73% for the second. Of course, it is Hallinan's and Wal-Mart's contention that the "deal" was that these experience modifiers would play no part in arriving at the premium to be paid by Wal-Mart. This is true even though they were sent to Wal-Mart by one of Hallinan's employees and included in the policies as the policies clearly provide that they should be.

During early 1984, apparently at Transit's request and demand, White & White Inspection Services, an independent auditing firm, was hired to audit the Wal-Mart payroll. In the fall of 1984, White & White concluded its audit and notified Miro of an increase in 1983 payroll from the purported $243,000,000 shown on the policy to $549,000,-

000. Miro applied this difference in payroll to the state rates on file in the various jurisdictions applied the experience modifier received earlier from NCCI of 1.70, and after applying applicable discounts, reached an additional premium figure of $6,028,894.

Between September and December of 1984, three meetings were held among Wal-Mart, Miro and A & A personnel concerning payment of this additional premium. It appears that Miro advised Sooter and Hallinan that he knew that the additional $6,000,000 premium was not really owed since the policy had been sold for a guaranteed premium of $3,500,000, but that, in order to satisfy certain statutory requirements, and to satisfy Transit, it was going to be necessary for it to be billed and shown as paid. He suggested that the way that this could be done would be for his company to bill Wal-Mart and for Wal-Mart to then pay the bill by wire transferring $6,000,000 to Miro at the Dallas bank with which it did business. These funds would then be transferred to Lafayette Re, which was Miro's reinsurance company owned by him, domiciled either in the Cayman Islands or on the Isle of Man. Lafayette Re would then retransfer the $6,000,000 to Wal-Mart as a "dividend." He said that since all of the parties involved did business with the same Dallas bank, this could be done in one day. Surprisingly, and in fact astoundingly, Sooter of Wal-Mart, after consulting with another officer of Wal-Mart, agreed that "this would be no problem" if they could be assured that their funds would not be at risk. There is a great deal of testimony by both Sooter and Hallinan about this proposed transaction, but it is not at all clear from this testimony what they believe or wish the court to believe the purpose of this

fake transfer was. Hallinan, for several pages of the transcript, testified that they only were told that the transfer was necessary to satisfy statutory requirements but they didn't know what those requirements were. Finally, in answer to the court's questions, after ducking and dodging for almost three transcript pages (pp. 6-160—6-162). Hallinan finally admitted that he saw no purpose for this illusory transfer other than to attempt to "fool someone." He finally admitted that he knew of no one that Miro, he, and Sooter would have any reason to "fool" other than Transit and regulatory authorities.

Sooter's testimony on this subject is not substantially more enlightening. Although he agrees that he and his superior, also an officer of Wal-Mart, decided "that should we be given the proper assurances that the money would flow through as described back to us that it probably wouldn't present a problem," he professes not to know what the purpose of the sham $6,000,000 transfer was. The best that he could do was to say that they (Miro and Hallinan told him that it was something that had to be done.

The fictitious transfer was not made because Miro's house of cards came tumbling down before it could be. Transit and Wal-Mart received word that Alexsis had not been reimbursed for claims paid by it in several weeks and was owed approximately $700,000. Transit subsequently cancelled Miro's authority and drew down the letter of credit that was established to guarantee the obligations of his reinsurance company. According to the testimony, the letter of credit was only $1.3 million.

In November-December of 1984, Transit learned that the reinsurers that had been paying claims under the Miro

program had stopped making payments. On December 4, 1984, Miro's agency was terminated by Transit.

On January 2, 1985, Muldoon sent an invoice for $13,000,000 additional premium for the Wal-Mart coverage to Hallinan. Hallinan did not forward the bill to Wal-Mart, or even tell Wal-Mart personnel about it. Instead, he returned it to Muldoon, advising that it was not in compliance with the "deal."

In mid-January of 1985, Alexander & Alexander advised Sooter that there would be a meeting in the New York offices of Muldoon. At the meeting, George Bowie, Chairman of the Board of Transit, announced that Wal-Mart owed Transit an additional $13,000,000 in premiums and that additional amounts would probably be owed in the future. He produced the invoice earlier sent to Hallinan, with a copy of the letter to Hallinan attached and demanded that the bill be paid in two weeks.

Sooter of Wal-Mart, after overcoming the shock occasioned by the bill and the fact that Hallinan had not told him of the earlier billing, returned to Bentonville, Arkansas, to consult with other officers of Wal-Mart. Bowie was advised by Wal-Mart personnel that the senior officers that would be required to make the decision were not in the office, and they requested additional time to advise Bowie of their decision. However, rather than advise Bowie of their decision, Wal-Mart quickly filed this action in Arkansas in an obvious atttempt to prevent suit from being filed against it in some other jurisdiction. .

The Receiver claimed during the trial that total losses paid on the two workers' compensation policies and the

tail coverage policy approximated $30,000,000, with approximately $21,000,000 of this being paid on the workers' compensation policies alone. Sooter testified (Tr. 2-68) that he believed this figure was too high, but admitted that payments on the policy were "somewhere in the neighborhood of sixteen to seventeen million dollars."

In respect to Sooter's sophistication in relation to insurance matters, he admitted (Tr. 2-70) that he had monitored the Texas self-insurance program for approximately three years. He recognized that that coverage required an audit and an adjustment of the premium based on the experience modifier. Wal-Mart had additional premiums to pay after the audits and application of the experience modifier, and he agreed that he saw such modifiers for each of the years on the Texas policy, but says that he had only a "vague understanding" of what an experience modifier was and how it applied. Then, with further cross-examination, it became obvious that he was fully aware of the purpose of these codifiers, and how they affected the premiums that Wal-Mart was required to pay on the Texas policy.

The court is particularly troubled by some of the testimony of Mr. Hallinan. Although, as indicated, he had over thirty years of experience in the insurance industry and, at least during part of the period, was receiving $6,000 a month to consult with Wal-Mart, he professed to have an amazing lack of knowledge about insurance matters. In addition, the court had a distinct feeling that Mr. Hallinan's testimony was less than credible. To see why, one only needs to read his cross-examination at Tr. 6-49 through Tr. 6-56. It took over six pages of transcript to

get him to finally admit that the purpose of depressing the payrolls as was done on both of the policies issued was to show regulatory authorities something that didn't exist. In other words, if the estimated payrolls of $547,000,000 on the first policy and $630,000,000 on the second policy were shown, it would be obvious to authorities with whom the policies had to be filed that the "deal" did not comply with requirements of law. After a great deal of sparring with the attorney examining him, the following question was asked and the following answer given:

> Q. All right. Now, Mr. Hallinan, isn't it a simple fact that since your testimony is that the way the rate structure is shown in the policy is not the way you're actually going to calculate policy premium has nothing to do with the way you're actually going to calculate the premium? That the only reason it was put in there with the wrong payroll is so that the state regulatory authorities would read it and say, well, that looks about right on a 3.5 million dollar premium?
>
> A. That's right .

Mr. Hallinan also testified that a "deal" for a $3.5 million premium on a payroll of $547,000,000 does not conform to state regulatory requirements, although it, again, took some "doing" to get him to say that. At Tr. 6-75 the following testimony is shown:

> Q. (By Mr. Sutton) Mr. Hallinan, you have referred to a contracted for maximum premium. And I don't know whether you claim that's what was done in this case or not; do you?
>
> A. Yes. There's an indication that a maximum premium would be available.

Q. And did you tell us on your deposition that that kind of a proposal does not conform to state regulations on standard workmen's compensation policies?

A. In this particular instance it is a different agreement.

Q. It does not conform to state regulatory authorities, does it?

A. Well, you're—it does conform to state regulatory requirements under the terms of the agreement.

Q. Which one? The one that was filed with the state regulatory authorities?

A. Well, yes.

Q. But a contract for a flat 3.5 million dollar premium on a payroll of 532 or 547 or 549 million dollars—

A. Right.

Q. —does not conform to the state regulatory authorities, does it, sir?

A. Not under that situation.

THE COURT: I'm not understanding. What did you say? Not under that situation?

THE WITNESS: Right.

THE COURT: Are you saying it does or it doesn't. I don't know what that answer means.

THE WITNESS: It doesn't.

THE COURT: It doesn't. All right.

There is other testimony, coming from the mouths of Wal-Mart's consultants, that the "deal" was not filed with regulatory authorities but the sham policies with depressed payrolls were filed instead because those involved

recognized that the "deal" would not be approved. At Tr. 6-163, Hallinan agreed that "you could not file in any state a 3.5 million dollar premium showing a $547,000,000 payroll." Paul F. Stanley, a vice president with Alexander & Alexander, with thirty-three years of insurance experience, the last twenty-two with Alexander & Alexander, was asked why "deals" such as the one in question in this case, were not filed with regulatory authorities. Although he did not appear to want to answer the question during the trial, it was obvious during impeachment by counsel for Transit, that he had testified in a deposition as follows:

> Q. Have you ever asked an underwriter why they don't put the agreement in the policy?
>
> A. As I believe I stated earlier, my assumption would be that the agreement is not entirely according to the filings that they have in all the statements [sic].

(Based on additional passage that were read from the depositions, it appears obvious that "statements" should read "states.") Then, in answer to questions asked by the court, Mr. Stanley testified:

> A. . . . All right. In this case I'm convinced the evidence shows that the first premium, the premium for the first policy, the '83-'84 was—at least I think there's plenty of evidence to indicate that Mr. Miro at least agreed with Wal-Mart and with A & A that the premiums would be $3.5 million. They then, I suspect used the $547 million payroll, divided that into 3.5 and came up with .6398. At least it looks like that's what happened.
>
> A. Right.

Q. It looks like .6398 had no relation to anything. Have you heard the testimony and had you looked at the file to see if that's a fact?

A. I've looked at the file. I don't recall the composite rate, but that's the way a composite rate of that sort would always be done, divide the premium by the estimated exposure.

Q. In other words, you do whatever you want to to arrive at what you think you can sell this policy for and then you—your composite rate is nothing more than the premium divided by the payroll.

A. That's correct.

Q. That's correct, and then in—or the next policy, '84-'85 I guess it would be, after a lot of negotiation the evidence shows having to do with whether or not some returned premium was due Wal-Mart, they said okay, we'll let you have it for the some 3.5, and I guess not too surprisingly they've merely—and I've done that on my calculator—they merely divided 3.5 by $630 million and says oh, that's 555555 ratio and that's what the composite rating is going to be. Is that the way you understand this was done in this case?

A. Yes, sir.

Q. All right. Forgetting again about what's "right" and "wrong", do you believe that the filing of any state allows a premium—or the law of any state allows a premium to be arrived at in those kinds of ways? In other words, take any state—let's take Arkansas for example. If you told Arkansas that's the way we arrive at this rate by filing, what do you think would happen?

A. I don't think that would be satisfactory to the regulators in Arkansas.

Q. Would it be satisfactory based on your 30 some years of experience—would that be satisfactory anywhere?

A. No, I doubt that it would, sir.

Q. Every state requires that you charge a premium for the business you write in that state based on the statute and on the filings that are on file. Is that correct?

A. Yes, sir.

Q. All right.

A. Again, within whatever latitude your accepted filings in that state gives you .

Q. Sure, sure, sure.

A. Yes, sir.

Q. In other words, if the evidence shows that in Arkansas for '83 and '84 they had deviations or a deduction, I'm not sure which one it was, but a deviation of 25% on file, what you'd have to do in order to be legal in Arkansas is apply the manual rates times the individual classifications of the payroll, apply the experience modifier to that and then deduct 25%.

A. That's correect.

Q. In other words, if you don't come up with a premium of at least that much you're not legal in Arkansas.

A. If you don't—yes, sir, that's correct.

Q. All right. The same kinds of things are done in all of the other states, or say at least similar things. You may have different filings as I understand it in other states, but the same kind of arithmetic has to be done in other states. It that correct?

A. Yes, sir and as I understand the way it's done it's the composite of all those under the various filings that end up being—they are used to back into the premium that was quoted to the client.

> Obviously if the premium quoted to the client is lower than the composite of all those can be justified, then the insurance underwriter who did it has a problem, but I've never in my experience had an underwriter come back and tell me that was the case.

The testimony of Jan Taylor, an employee of the Arkansas Department of Insurance since 1979, was particularly helpful to the court. At the time of her testimony, Ms. Taylor was the Director of the Division of the Arkansas Department of Insurance responsible for reviewing contracts that property and casualty insurers issue in Arkansas, including workers' compensation insurance.

Among other things, Ms. Taylor described that workers' compensation insurance is social insurance and is regulated by the state of Arkansas, although controls had been reduced somewhat in recent years. However, it was her testimony that her department still had the responsibility of reviewing and approving or disapproving rate rule and form filings made by insurance carriers who desired to write insurance in Arkansas. She testified that Arkansas is a "prior approval state" which means that an insurance carrier must have prior approval of its rates and policies before issuing such policies in Arkansas. She testified that it was the department's duty to see that filings made and policies issued and rates agreed upon were not exeessive, unfairly discriminatory, or inadequate. She said that the department had a duty to attempt to prevent carriers from treating one insured "different from another insured."

Ms. Taylor was asked: "What types of things have to be approved before they are used for workers' compensation in Arkansas?" Her answer was:

Every aspect of workers' compensation has to receive approval. Some of it can be done by the National Council on Compensation Insurance for their companies like coming up with a new job classification, but that does receive prior approval. The prices going to be charged to the insurer has to receive, we're talking about the front end price going out according to the risk, has to receive prior approval. Any sort of departure from anything previously on file has to receive approval.

She described that companies issuing policies in Arkansas could choose to adopt rates promulgated by the National Council on Compensation Insurance. She described the function of this Council as follows:

A. Because of the social nature of workers' compensation and because there are so many jobs performed by workers across the United States it's important for insurance companies who provide workers' compensation insurance to employers to have some kind of credible data so that they can use it as a point to determine how much they need to charge when they're going to issue policies to Dillards who has some clerical workers and has some retail salespersons, they have some drivers. All of these job classifications for across the United States are all reported together so if this is Class A-120 for instance, we'll have the experience of everybody that falls into that across the United States from all the insurance companies writing that. They take that and they weigh each one for the various states, in other words we may have an awful lot of credibility, we have a lot of clerical workers in Arkansas. There are some classes that we have very little credibility for and an insurance company wants to come in and write this in a state will need some idea how much they need to charge for that classi-

fication. The National Council collects the data and promulgates the rate that's going to be used for every job classification basically.

THE COURT: You say there's something over 600 jobs in the classes?

BY MR. TURNER:

Q. Now in Arkansas it's my understanding that they're not required to follow the National Council on Compensation, is that right?

A. Yes.

Q. Now if an insurance company desires to adopt what the National Council has promulgated as far as these national rates go, in other words if they want to use what the National Council has promulgated, how would they go about doing that in Arkansas?

A. They would generate a letter to the insurance department saying they're going to use the rates and rating plans on file by the National Council.

Q. Now let's go back to the years of 1983 and 1984. Are you familiar enough with filings that were in Defendant's Exhibit #3 and could you tell the jury during that period of time whether Transit Casualty was a member of the NCCI in Arkansas.

A. Yes, they were a member of NCCI.

Q. Okay. Now once you become a member of the National Council in Arkansas, and you're writing workers' compensation insurance, and you want to modify this rate which is made by the National Council, you want to change it say from 110 to 115, can an agent for an insurance company or an insurance company just begin applying a different rate or must they first notify the Insurance Commissioner's office?

A. If they're going to use a member of NCCI and they have filed to use NCCI and they're not going to use $1.10 which is what NCCI had for that class code, they would have to file a request to use something other than $1.10.

Ms. Taylor testified that Transit had on file the deviations and scheduled rating plans introduced as Plaintiff's Exhibits 27, 28 and 29, with the effective dates shown, but that if any of these were to apply to a specific policy, it should be shown on the policy issued.

In answer to questions by Transit's counsel, Ms. Taylor said that she knew of no basis for writing workers' compensation insurance and calculating the premium other than on the basis of the expected payroll. The premium is calculated by breaking the estimated payroll down into the various job classifications, and then for NCCI companies, applying the rate for each job classification to the payroll for that category. To that is applied, at a subsequent time, the experience modifier developed by the NCCI. At Tr. 3-149, she testified:

Q. In those seven years, Ms. Taylor, have you ever had the opportunity or the occasion to run into a situation where a workers' compensation policy which is standard, has got the NCCI rates, it's got the appropriate payroll and it's got the experience modifier attached to it and endorsement and it's got everything that complies with what these statutory requirements are and that policy has been furnished to the insured but there's been some kind of side deal cut that alters the premium. Have you ever run into that?

A. I assume you mean a side deal—no.

Q. And that's not something that you would consider as being to the insurance department something

that's common in the insurance industry, would you?

A. As far as we know?

Q. As far as you know.

A. I would have to say no.

Q. In fact is a side deal—if the determined premium is different than what's been furnished to the insurance commissioner's office and the rates used are not on file, those are incorrect, are they not?

A. Using a rate other than that filed is incorrect.

She said that she had never seen a "composite rate" used in workers' compensation insurance. In respect to the "deal" which Miro made with Wal-Mart, she testified:

Q. Okay. Now, when we're talking about a composite rate we're talking about a rate for job classifications kind of like this rate right here for clerical, are we not?

A. I'm not sure what you're talking about in workers' compensation. I assume you are talking about combining all of the factors that go into it and using a composite rate.

Q. Okay. If you combined all of the factors for let's say clerical and I think you mentioned some number about in the different classifications there are but if you combined all of those average numbers, would that in someway reflect what it should reflect when you use them in the correct way by listing them separately? Do you understand my question?

A. No, I don't.

Q. Okay. I'm having a hard time. What I'm trying to say is if you use 100 classifications and 100 manual rates you come to some figure and then

you used a composite rate and came to some figure, that messes up the whole procedure, does it not?

A. I don't think we would accept that.

Q. Okay. Now, let me show you a formula which has been called a rating formula as we've been discussing. On this blow up right here—can you see that from there? I can bring it closer.

A. It's alright.

Q. It says right here, earned premium equals chargable losses minus investment income over one minus six cost factor. Let me ask you if you have ever seen in your experience in the workers' comp. department down in Little Rock—have you ever seen a formula for workers' compensation rating anything like this?

A. No. Those things are used by the National Council to come up with the manual rate but their fixed cost factor—the earned premium of the losses, investment income, but not for developing a premium on an individual risk.

Q. If this formula right here, prior to either one of these policies being issued, if that formula had been submitted to your office to be approved on behalf of Wal-Mart—I mean on behalf of Transit Casualty for the Wal-Mart account, would it have been approved?

A. I don't think—I would say that we would have a lot of reservations, that we would probably spend quite a bit of time looking at it. It would not have been automatically approved, no.

Q. Out of the three standards that you described to us earlier today—

A. Uh-huh.

Q. —the unfairly discriminatory, inadequate and excessive, could you tell me what problems you would have with that formula right there?

A. I think you might have all three of them with that formula. Unfairly discriminatory because, you know, I assume it would be for one insured, and excessive because—do you want me to go ahead? Excessive because the—I can't really see it but I believe it has a fixed cost factor in theinvestment income. I'm not sure how you would pro rate that out for Transit Casualty when they're already included in the manual rates, the figures that are used by the National Council and could be inadequate, I don't know, it just depends on what numbers they plugged there and how they segregated that account out.

The "proof" in relation to the amounts owed according to the policies of workers' compensation insurance as issued came from Frank R. Watkins who until June of 1986 was with Transit Casualty Company or its Receiver. When Transit was a solvent company, he was a Vice President in the Underwriting Department and, among other things, it was his duty to calculate premiums on workers' compensation policies. He prepared defendant's exhibit 40 which is a summary of his calculations showing the amounts that the Receiver claims Wal-Mart owes on the two policies. He says that he reviewed Transit's filings in all applicable jurisdictions and applied deviations on file. In fact, he testified that he applied the 15% deviation in Arkansas which was filed a few days before the initial policy was issued, even though it was not shown on that policy by Miro. In addition, he applied the relevant experience modifiers and discounts and computed the premiums shown on defendant's exhibit 40 using standard

underwriting guidelines. Although Wal-Mart, through its attorneys, contends that these figures are not accurate, no evidence was offered by it to refute them.

Calculated in the manner described by Watkins, he testified that Wal-Mart owed an additional premium of $9,696,845 on the first policy, when the payroll determined by the White & White audit is used, and $7,505,378 if the payroll thatWal-Mart contends was the correct one is used. On the policy for the second year, he testified that the additional premium due is $9,266,766. Thus, according to these figures, Wal-Mart either owes an additional premium of $16,772,144 if the Wal-Mart payroll figures are used for the first year and the White & White audit figures for the second, or $18,963,611 if the White & White payroll audit figures are used for both years.

III. Did Carlos Do It?

As indicated by the facts set forth in the preceding section, the evidence shows that Carlos Miro agreed with Wal-Mart to provide workers' compensation coverage for Wal-Mart in all of the states in which it did business for a flat and guaranteed premium of $3,500,000, to be affected by no other factors, for both of the years in question. It is also clear that, rather than show the "deal" entered into, undoubtedly, as will be discussed below, because it was obviously not in compliance with the law of any state, Miro prepared and forwarded to Hallinan for his review and acceptance standard workers' compensation insurance policies showing premium calculations which, if one was not aware of the depressed payroll shown, would comply with the laws of the states in which Wal-Mart had employees. Hallinan reviewed the policies, accepted them, and

forwarded them on to John Sooter of Wal-Mart. This was done by Miro and accepted by Hallinan and, in fact, Sooter, even though none of the three believed for one moment that the policy correctly reflected the "deal." Hallinan apparently accepted it and sent it on to Wal-Mart because he believed that this was "common practice." In other words, his excuse was that "everybody does it."

Prior to and during the trial, Transit contended that Wal-Mart was bound by the terms of the insurance policies delivered and accepted, and it objected on the basis of the parol evidence rule to any evidence being offered and received to show the "deal". At the start of the trial, the court ruled that the parol evidence rule did not apply, and, after hearing the evidence, the court is even more convinced that it does not. The court does not believe that anyone involved in the transactions or, in fact, anyone in the courtroom during the trial, really believes that the policies reflected the arrangement reached by the parties. The policies delivered were shams to show someone (and it must have been regulatory authorities) that policies had been issued which complied with the law of the states in which they had to be filed and reviewed.

Arkansas law permits parol evidence to show, among other things, that the written agreement is not really the agreement of the parties and what the parties in fact intended their agreement to be. *See L.L. Cole & Son, Inc. v. Hickman,* 282 Ark. 6, 665 S.W.2d 278 (1984); *Jefferson Square, Inc. v. Hart Shoes, Inc.,* 239 Ark. 129, 388 S.W.2d 902 (1965); *Kyser v. T.M. Bragg & Sons,* 228 Ark. 578, 309 S.W.2d 198 (1958). Parol evidence is always permitted where "there is a question of whether the parties intended

to integrate their entire agreement into the document involved in the case." *Starling v. Valmac Industries, Inc.*, 589 F.2d 382, 386 (8th Cir.1979), *citing Farmers Coop. Ass'n v. Garrison*, 248 Ark. 948, 454 S.W.2d 644 (1976), *citing 3 Corbin on Contracts* § 573 (1960); *see also* 30 Am. Jur.2d *Evidence* § 1034 (1967).

In this respect, Transit contends that the "sham theory" which allows parol evidence to show that the writing is a "sham" is not applicable where parol evidence is offered to negate a legal contract and prove the terms of an illegal contract where the "real agreement" was made for the illegal or immoral purpose of deceiving or misleading public authorities or is contrary to public policy. *See Bank of America Nat. Trust & Sav. Assoc. v. Gillaizeau*, 593 F.Supp. 239 (S.D.N.Y.1984); *Bersani v. General Accident F. & L. Assur. Co.*, 36 N.Y.2d 457, 369 N.Y.S.2d 108, 330 N.E.2d 68 (N.Y.1975); *Kergil v. Central Oregon Fir Supply Co.*, 213 Or. 186, 323 P.2d 947 (1958); 30 Am.Jur.2d *Evidence* § 1034 (Supp.1986). While this argument is not without merit, the court believes that that contention can be more logically and properly discussed in the section below which discusses the enforceability of the "deal." As indicated, the court believes that the evidence was admissible. The question of whether it should be considered by the court to prove an illegal or immoral contract or one against public policy is another question.

In short, the court is convinced that, in fact, Carlos Miro did exactly what Wal-Mart charges him with doing. He agreed to provide Wal-Mart's workers' compensation coverage for two years at a flat $3,500,000 per year, to be

affected by nothing. In addition, he provided retroactive coverage, agreeing to pay any workers' compensation claims, whether known or unknown, arising in any of the Wal-Mart locations during the period from February 1, 1980, to January 31, 1983. He agreed to accept this liability, both known and unknown, for the amount of reserves set up by Wal-Mart's adjusters at the time the known claims were filed. In addition, he agreed to insure general liability claims at any Wal-Mart location, both known or unknown, which resulted from any incident occurring between February 1, 1980, and January 31, 1983.

Thus, the answer to the question posed at the beginning of this section, "Did Carlos Do It," is unquestionably "yes."

IV. Did Carlos Have Authority To Do It?

There is no question but that Carlos Miro was an agent of Transit Casualty Company wth the power to issue Transit policies. In fact, the evidence shows that he was provided by Muldoon, acting in Transit's behalf, blank prenumbered policies to use for that purpose. An agreement was entered into between Miro and Muldoon acting in behalf of Transit. (Plaintiff's Ex. 19). Article I, subparagraph (a), specifically sets forth the actual authority granted by Transit to Miro. He was authorized to issue policies of insurance "subject to and in accordance with the insurance laws and regulations of each State, and in accordance with rates, filings, forms, policy limits, underwriting, guidelines governing acceptance . . . all as directed, filed, and promulgated by the Company . . . utilizing rates filed by the Company."

The court believes that it is abundantly clear from the evidence in this case that Miro acted well outside the bounds of the actual authority granted to him. Unquestionably, he agreed to provide workers' compensation coverage which, in the court's view, as will be discussed below, is not in accordance with the insurance laws and regulations of any state in which Wal-Mart did business, and, the rates used clearly were not filed in any state and, in fact, could not be. Both of the officers of Wal-Mart's $6,000 per month consultant who testified, with combined experience in the insurance industry of over sixty years, said that the "deal" could not have been filed and approved in any state of which they were aware.

Since Miro exceeded his actual authority, the question then becomes whether he had apparent authority to enter into the "deal." This court had occasion to consider the issue of apparent authority in *Scholtes v. Signal Delivery Service, Inc.*, 54 8F.Supp. 487 (W.D.Ark.1982). In that case, we said that, in Arkansas, apparent authority is defined as follows:

> Apparent authority is such authority as a principal proclaims or permits, such authority which a principal by lack of care causes or allows, or such authority as a reasonably prudent man using diligence and discretion would naturally suppose. (citations omitted). The principal's liability attaches regardless whether the authority was actual or apparent, so long as the third party acts in good faith.

Id. at 495. *See also Arkansas Valley Feed Mills, Inc. v. Fox De Luxe Foods, Inc.*, 171 F.Supp. 145 (W.D.Ark. 1959), *aff'd*, 273 F.2d 804 (8th Cir.1960); *Mack v. Scott*, 230 Ark. 510, 323 S.W.2d 929 (1959).

Thus, the law in Arkansas is that a showing of "apparent authority" requires both (1) conduct by the principal and (2) a reasonable belief by the third party dealing with the agent that the agent has the authority to do what he is doing. In this case, it is true that Transit made blank policies available to Miro and authorized him to issue them so long as he complied with the conditions set forth in the agreement discussed above. That is clear. The hard question is whether that conduct by Transit would cause a reasonable person to believe that Miro had authority to issue policies of workers' compensation insurance using a rate structure that even Wal-Mart's "experts" did not believe could be openly filed in any state.

It should be remembered that the insured in this case is Wal-Mart. We are not talking about a mom and pop five and dime on the corner of First and Main. Instead, we are talking about a company which, according to the authors of the popular book, *In Search of Excellence—Lessons from America's Best-Run Companies,* "is the mass retailing success story of the late 1970s and the early 1980's." T. Peters & R. Waterman, Jr., *In Search of Excellence—Lessons from America's Best-Run Companies,* 191-192 (1982). We are talking about a corporation that everyone in northwest Arkansas knows started as a small discount operation in northwest Arkansas and during the succeeding few years developed into one of the top three or four retailers in America. This is a corporation that almost anyone writing on modern day success stories includes in the story. It is considered, as evidenced by the discussion of Wal-Mart in the book cited above, to be one of the best-run businesses in all of this country and, in fact, there is rarely a discussion in books, magazines and

newspapers about modern day business success stories that Wal-Mart and its founder, Sam Walton, are not given prominent and laudatory discussion.

Not only is Wal-Mart one of the best-run companies in America, the evidence in this case indicates that it had a whole department with a director that did nothing but look out after Wal-Mart's insurance interests. While Sooter, during the course of the trial, appeared to be attempting to convince the court that he knew little about insurance, the court does not believe for a moment that he was not a sophisticated and astute businessman knowledgeable in the area of insurance. If he was not, he would not have been Director of the Risk Management Division of Wal-Mart. Paul Stanley, Vice President of Wal-Mart's consulting firm, thought that he was. In a deposition given, a portion of which was read to him during the cross-examination of him at the trial, he said, "I would say in every case—we are dealing with rather sophisticated people such as Mr. Sooter and other risk managers and I can't get into their heads . . . ."

The evidence in this case indicates that Sooter had been the Director of the Risk Management Department of Wal-Mart for almost two and one-half years at the time of the negotiation of the first contract. The evidence indicates that Wal-Mart, prior to the Miro policy being issued, had been self-insured in most states and had a standard policy in the state of Texas. During the two and one-half years that Sooter had been the Director of Risk Management, he had monitored and been responsible for the proper operation of not only the self-insurance program but also the Texas program insured by a standard policy. He admitted, somewhat reluctantly, that he was

aware of experience modifiers and how they were applied to calculate premiums. He was responsible for the self-insurance program so he must have been aware of Wal-Mart's loss history. The court simply does not believe that he really believed at the time that he entered into the "deal" with Miro that it was permissible and would be accepted in any state in which Wal-Mart did business. If he had believed that that was the case, why did he accept a policy of insurance that clearly did not set forth the agreement that he contends he reached? Why did he accept a policy that had depressed payrolls? Was it because Hallinan told him that that is "common practice" and not to worry about it? If that is the case, was that reasonable for a man of Sooter's business experience and expertise? The court believes that mom and pop on the corner would know that they should question a policy of insurance which doesn't even come close to properly setting forth the agreement that was reached in relation to the insurance coverage. As indicated, the "deal" was that the insurance would be provided for $3.5 million per year, not affected by anything. The policy that Sooter got and accepted clearly provided otherwise. It was clearly a standard policy, and it provided that the premiums would be calculated using the NCCI manual rates and would be adjusted by experience modifiers.

Sooter's testimony is that he made one deal but that he received and accepted something entirely different. Someone with much less business experience and business acumen than that displayed by Sooter should have worried about that even if his expert told him not to.

An event occurred during the second policy year which the court believes indicates that Sooter and the A & A

people knew that the "deal" was not one that would, in the words of one of the A & A executives "pass muster" in any state. The court has reference to the $6,000,000 sham transfer that was agreed to and did not take place only because Miro's activities were discovered and the house of cards that he, Wal-Mart and Hallinan built came tumbling down before the transfer could take place.

Wal-Mart, in its brief, contends that this was a "non-event" and should have no bearing on the outcome of this case. The court disagrees. It is recognized that the transfer did not, for the reasons stated, take place, but the court is convinced that the fact that Wal-Mart's executives agreed to the transfer speaks volumes about their knowledge of whether the deal was a proper one insofar as state regulatory authorities were concerned. At Transit's insistence, Miro had the Wal-Mart account audited by White & White. The audit, when policy provisions were applied, showed that Wal-Mart owed an additional premium in excess of $6,000,000. Miro said to Hallinan and Sooter that he had a plan to get around this problem. His plan was that a sham transfer of $6,000,000 would take place. Miro would bill Wal-Mart for the additional premium and Wal-Mart would wire transfer $6,000,000 to Miro & Associates in Dallas which would then transfer the money to its reinsurance company which was domiciled either on Cayman Island or the Isle of Man. That reinsurance company would, the same day, transfer the funds back to Wal-Mart. Astoundingly, Sooter and his boss, an executive with Wal-Mart, agreed to this fake transfer and it is obvious that their only concern was that their funds not be "at risk."

The court believes that anyone reading the portion of Sooter's and Hallinan's testimony on this transfer would

have to believe that they must have known more about the purpose of this than they now would like to admit. Their testimony is that Miro simply told them that it was to satisfy a "statutory requirement." They say that they did not know what that meant and they waited for Miro's lawyer to tell them, but he never did. The court simply does not believe that. The court is convinced that astute and experienced businessmen of the caliber of John Sooter and George Hallinan must have known that this could have no other purpose than to "fool someone." In fact, under questioning by the court, Hallinan admitted as much. What other purpose could it have had? If Sooter and Hallinan really believed that the deal was a legal one, why the sham transfer? Could it have had any other purpose than to attempt to show someone that something occurred which didn't? Since the answer to that question is obvious, who could Sooter, Hallinan and Miro have been intending to "fool"? Could it have been anyone other than either Transit or state regulatory authorities? Hallinan agreed that it could not. The court can see no other explanation for this unexplainable conduct than that Sooter and Hallinan must have known that their "deal" did not comply with the law of any state and that that fact must be "covered up."

Even if it assumed for the sake of argument, that John Sooter did not know this, an assumption that stretches this court's credulity considerably past the breaking point, it is clear that the consultants which he paid, at least during part of the relevant period, $6,000.00 per month did. They said that they did. (Hallinan Tr. 6-163 and Stanley Tr. 7-128). It has long been the law in Arkansas that "the principal is affected with notice of all his agent knows

in the line of his duty or the scope of his powers." *Whitehead v. Wells*, 29 Ark. 99 (1874), and other cases cited in West's *Arkansas Digest* Key No. 177(1). It is also well settled that a third person, by undertaking to deal with a purported agent, is put on inquiry as to the extent and scope of the agent's authority and must use due care to discover the authority or else suffer the consequences if it is exceeded. *See also International Harvester Co. v. McLaughlin*, 182 Ark. 1122, 34 S.W.2d 452 (1931); *J.T. Fargason Co. v. Dudley*, 173 Ark. 1148, 294 S.W. 6 (1927); *Hadley Milling Co. v. Kelly*, 117 Ark. 173, 174 S.W. 227 (1915); and 2A C.J.S. *Agency* § 168 (1972).

Applying the law, and considering what the court is convinced John Sooter knew and what the law imputes to him from Hallinan's and Stanley's knowledge, the court finds that it was not reasonable for him to believe, if he in fact did, that Miro had the authority to issue policies of insurance which would not comply with the filing requirements of any state. Thus, Miro did not have either actual or apparent authority to make the "deal" that he made with Wal-Mart.

The court is further convinced that John Sooter either knew or certainly should have known that he did not. The evidence, in the court's view, indicates that Sooter quickly recognized what a deal he was getting when he received the bid on the Texas only insurance. He promptly asked Hallinan to have Miro bid on all of their coverage. There is nothing wrong with that, but Sooter, like most of us, should have learned long ago that, whether it is a man in a pickup truck wanting to pave your driveway or roof your house, or someone on the telephone trying to sell you a lot

in Florida, if the deal sounds "too good to be true," it probably is.

Did Carlos have authority to do it? The answer is "no" and it was not reasonable for Sooter and Hallinan to think that he did.

V. Is The "Deal" Enforceable?

Workers' compensation insurance is social insurance not only required but also controlled by legislative enactments in every state. It has the salutary purpose of protecting employees, employers and the public by providing a means by which injured workers may be compensated during the period of their inability to work caused by the injury so that they may continue to exist and feed their families. The public is protected because, hopefully, this prevents injured workers from becoming wards of the state maintained at the expense of the public. Besides, it is the "right thing to do."

An overriding and compelling state interest has been recognized for many years and is well expressed in *Employer's L.A. Corp. v. Success-Uncle Sam Cone Co.*, 124 Misc. 614, 208 N.Y.S. 510 (1925). That court said:

> It should be borne in mind that the policy of the state, as expressed in sections 67 and 141 of the Insurance Law, is to remove the matter of rates, premiums, and classifications from the field of private bargaining and agreement. Section 67 of the Insurance Law does this by providing that no rates shall take effect until approved by the superintendent of insurance, and thus limits the power of the insurance company and the insured to contract on the basis of one rate alone—the rate approved by the superintendent of insurance.

> This policy has a threefold purpose: First, to protect injured workmen and the dependents of those killed in industrial accidents, by insuring the financial stability of companies writing compensation insurance. This means the maintenance of adequate reserves on the basis of a sound and scientific system of rates carefully supervised by the state. Secondly, it has for its purpose the protection of employers against excessive rates, and it is the state's duty to afford this protection because employers for the most part are compelled by law to carry workmen's compensation insurance; they have no choice in the matter, except that certain large employers may under prescribed conditions carry their own insurance. And finally this policy was designed to guard against rebates, discriminations, and favoritism in rates, the effect of which would be harmful to employers as well as to injured workmen.

Id. 208 N.Y.S. at 512. *See also Public Service Mut. Ins. Co. v. Rosebon Realty Corp.*, 39 Misc.2d 663, 241 N.Y.S.2d 555 (1963).[1]

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1. *See also American Mut. Liability Ins. Co. v. Plywood-Plastics Corp.*, 81 F.Supp. 157 (E.D.S.C.1948); *Contractor's Safety Assoc. v. California Comp. Ins. Co.*, 48 Cal.2d 71, 307 P2d 626 (1957); *Key System Transit Lines v. Pacific Employers Insurance Co.*, 52 Cal.2d 800, 345 P.2d 257 (1959); *Great American Ins. Co. v. Nova-Frost, Inc.*, 362 N.W.2d 358 (Minn.App.1985); *Employers' Liability Assur. Corp. v. Arthur Morgan Trucking Co.*, 236 Mo.App. 445, 156 S.W.2d 9 (1941); *Public Service Mutual Ins. Co. v. Rosebon Realty Corp.*, 39 Misc.2d 663, 241 N.Y.S.2d 555 (1963); *Warm Springs Forest Products Ind. v. Employee Benefits Ins. Co.*, 74 Or.App. 422, 703 P.2d 1008 (1985); *Mountain Fir Lbr. Co. v. Employee Benefits Ins. Co.*, 296 Or. 639, 679 P.2d 296 (1984); *Glenn H. McCarthy, Inc. v. Knox*, 186 S.W.2d 832 (Tex.Civ.App.1945); *Associated Employer's Lloyds v. Dillingham*, 262 S.W.2d 544 (Tex.Civ.App. 1953).

Although there is some dispute about what law applies in determining whether the insurance contracts in this case are enforceable, the court believes that the law in Arkansas on this subject is substantially similar to the law in each of the other states in which Wal-Mart did business during the relevant period. In addition, as already indicated, the court is convinced that the evidence shows that the "deal" entered into in this case would not be acceptable in any relevant state. Since that is true, it is not necessary for the court to determine whether the law of Arkansas or some other state applies. A choice-of-law analysis cannot begin until a specific issue has been found where laws conflict. *Snow v. Admiral Ins. Co.*, 612 F. Supp. 206, 208-10, (W.D.Ark.1985). Absent a real issue of conflicting laws, a court need not determine what "contacts" are relevant to a choice-of-law analysis. Acting otherwise would be responding to a "false conflict." *See generally* Restatement (Second) of Conflicts §§ 181-188 (1971).

Every relevant state requires that employers who meet certain criteria make provisions to protect their workers in the event of injury. Arkansas, nor any other state, gives the employers a choice about whether they desire such protection. They must have it. Likewise, the states do not give the employers a choice as to the amount of coverage that they will have. Instead, the law requires, not only that they provide such protection, but the level of protection that must exist. The law specifically sets forth the benefits that are payable in relation to injuries, and the employer may not choose to provide something different. For example, he cannot say that he does not believe that his clerical workers, or some other class of

workers, are not substantially at risk, so he won't make provisions to protect them. He must protect each worker at the level of protection required by the law of the applicable state.

Not only do the states provide that the employer must have such protection, every state, in one manner or another, provides what the employer will pay for it. In most instances at least, and the court believes in every state in which Wal-Mart did business during the relevant period, the amount that the employer pays for the insurance must be first approved in some manner by regulatory authorities. In other words, the employer is required by the state to carry insurance, and the state dictates the rates to be charged. It is true that, in recent years, more leeway has been granted in this respect, but the fact appears to be that every state relevant to the issues in this case still maintains substantial control over the making and charging of rates for workers' compensation insurance.

For example, in Arkansas, Ark.Stat.Ann. § 66-3120 (Repl.1980) requires all workers compensation carriers to file rates, forms, rating plans and manuals with the Arkansas Insurance Commissioner's office for prior approval. The statute mandates that any rate or method of premium development for workers' compensation be on file with and approved by the Insurance Commissioner's office before it is offered. As Ms. Taylor testified, the purpose of this is to protect workmen and the public by ensuring that carriers do not unfairly discriminate between employers or charge excessive or inadequate rates. The court believes that it is obvious that this is a legitimate concern of the regulatory authorities.

Obviously, in order to protect the workmen and the public, the insurance provided must be "fair." It would not be "right" to allow an employer such as Wal-Mart, because of its immense size and bargaining power, to obtain insurance for an inadequate rate. Obviously, someone must pay under those circumstances, and it has to be either the public or other employers. The regulatory authorities are concerned that the rates be adequate because, if they are not, the insurance carrier providing the coverage often "goes broke" as Transit did, leaving someone else "holding the bag."

As indicated, Wal-Mart appears to contend that Arkansas law should not be applied to this matter in determining whether the "deal" is enforceable, but fails to say what law should be applied. In fact, all states listed in the insurance policies issued have similar legislation to that of Arkansas.[2]

In Arkansas, and it appears in the other states relevant to the issues, an employer may choose the NCCI to establish the basic formula for determination of the premiums. According to Ms. Taylor, the NCCI promulgates standard rates for over 600 job classifications. As Ms. Tay-

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2. Ala.Code § 27-13-29 (1975); Ark.Stat.Ann. § 66-3120 (Repl. 1980); Fla.Stat.Ann. § 627.091 (West 1984); Ga.Code Ann. § 34-9-130 (1982); Ill.Ann.Stat. ch. 73, ¶ 1065.4 (1965); Ind. Code § 27-7-2-10 (Burns 1986); Iowa Code Ann. § 515A.6 (1949); Kan.Stat.Ann. § 40-1113 (1986); Ky.Rev.Stat.Ann. § 304.-13-040 (1980); La.Rev.Stat.Ann. § 22-1407 (West 1978); Miss. Code Ann. § 83-3-107 (1972); Mo.Rev.Stat. § 287.320 (Supp. 1986); Neb.Rev.Stat. § 44-1403 (1984); N.M.Stat. Ann. § 59A-17-10 (1978); N.C.Gen.Stat. § 58-124.20 (1982); Okla.Stat.Ann. tit. 36, § 901 *et seq.* (1976) S.C.Code Ann. § 38-43-330 (Law. Co-op 1984); Tenn.Code Ann. § 56-5-306 (Supp.1986); Tex. Ins.Code Ann. § 5.60 (Vernon 1981).

lor explained, if an employer chooses to use NCCI rates, it must do so unless prior approval is obtained from the regulatory agency. If a policy is issued under these conditions, the premium to be charged is determined by breaking the estimated payroll down into the relevant job categories, and then applying by a simple mathematical calculation the NCCI rates to the estimated payroll for each category. If the employer is large enough, an experience modifier is later established by the NCCI to reflect each insured's actual experience in the various states. If the insured's experience modifier is greater than 1.00, the insured is required to pay additional premiums to cover its bad loss experience. The obvious intention of this is to encourage loss prevention techniques and to promote equality among insureds. Logically, if Wal-Mart's loss experience is 70% or 73% worse than the average, Wal-Mart should pay more. If it does not, someone does and obviously, in most cases at least, it has to be the employers who do a better job in containing losses than Wal-Mart does. Ultimately, of course, the public pays. This system insures that other employers and the public are not required to pay the "tab" because a particular employer is a sharper negotiator or has more bargaining power than others and is, thus, able to "beat down" the premium.

In Arkansas, and other states, the final step in premium development is a premium discount which is applicable if the premium developed is of sufficient amount. According to Ms. Taylor, these discounts are intended to provide credits to large insureds to recognize legitimate cost savings based upon lower per capita handling costs.

Employers who choose to use NCCI are also permitted, under proper circumstances, to take advantage of cer-

tain retrospective rating plans provided by NCCI. There are five retrospective rating plans provided, and they are based on the standard formula, but permit credits based on the insured's actual loss experience. The maximum premium is still calculated utilizing the standard formula, but it is reflected as a percentage of a standard premium. These plans still have requirements for maximums and minimums, and they utilize manual rates and experience modifiers and must be reflected in the policy and an applicable endorsement approved by the regulatory authority. They must be applied to legitimate estimated payrolls and cannot be manipulated, as was done in this case, to arrive at a premium already agreed to.

In recent years at least, Arkansas, and most other states, have relaxed the regulation of workers' compensation rates to some extent. In most states, an insurance company may deviate from the manual rates and rating plans by filing a proposed deviation or modified rating plan to be approved by the Insurance Commissioner's office. However, these plans cannot be discriminatory and the regulatory authorities in the states review them to ensure that they are not. Once approved, the deviation or modification can be utilized to develop premiums if it is reflected in the policy itself. According to Ms. Taylor, if such plans are not approved, the carrier is required to use the standard formula discussed above.

Ms. Taylor testified that, according to the department's records, Transit was a member of NCCI and had the plans or deviations introduced as Plaintiff's Exhibits 27, 28 and 29 on file with the effective dates shown. However, Ms. Taylor advised that if these deviations or plans

were to be used, it should be shown on the policy. In this respect, the court believes that the evidence shows, unequivocally, that no one who had anything to do with developing the premiums in this case relied to any degree on these deviations or plans. It seems to be Wal-Mart's position that the insurer could have if it had wanted to, but the fact remains that it did not, and no one has any reason to believe that it did. The "deal" was that the premium would be $3.5 million, irrespective of any other factors.

It was Ms. Taylor's testimony, and it appears to be true in every other state, that after the initial premium is calculated as outlined above, the final premium to be paid by the insured is subject to adjustment by audit following the policy period. If the estimated payroll is less than the audited payroll, the insured pays additional premiums based on the applicable state rates, experience modifiers and discounts.

Arkansas has a statute which, in the court's view, makes it clear that a policy of insurance issued must reflect the true "deal" made between the insured and the insurance carrier. Ark.Stat.Ann. § 66-3019 has been called an anti-rebate statute, but in the court's view, it is much more than that. As indicated above, the court believes that, in Arkansas, and most other states, the legislature not only provides what coverage the employers of the state will have, but also what they must pay for it. This statute very effectively carries out this legislative purpose. It provides in pertinent part:

> (1) No property, casualty or surety insurer or any employee thereof, and no broker, agent, or solicitor shall pay, allow, or give or offer to pay, allow or give, directly or indirectly, as an inducement to in-

surance or after insurance has been effected, any rebate, discount, abatement, credit or reduction of the premium named in a policy of insurance, or any special favor or advantage in the dividends or other benefits to accrue thereon, or any valuable consideration or inducement whatever not specified in the policy, except to the extent provided for in an applicable filing with the Commissioner as provided by law.

(2) No insured named in a policy, nor any employee of such insured, shall knowingly receive or accept, directly or indirectly, any such rebate, discount, abatement, credit or reduction of premium, or any such special favor or advantage or valuable consideration or inducement.

The court believes that this statute was intended to any clearly and unambiguously does provide what the insurer will charge for an insurance policy, and what the insured must pay for it. It leaves no alternative. It says that the insurance carrier must charge the premium shown on the policy and that the insured will not knowingly pay anything other than the premium shown unless there are applicable filings authorizing a premium other than that shown.

In this case, the policies in question showed a premium which, at least on its face, complied with state law. The fact is that we now know that it didn't because Miro depressed the payrolls and Sooter and Hallinan, although recognizing it, accepted it because it was "common practice." But the fact is that the policies, as issued and accepted, provide for the proper manner for calculating the premiums to be charged. These policies clearly and unambiguously say that it is recognized that the preimums shown on the face of the policies are estimated only, and

that the final premium will be determined by an audit and an application of experience modifiers when available.

Thus, Ark.Stat.Ann. § 66-3019 directs Transit to charge the premium shown on the policies, and gives it no alternative but to do so. Similarly, this statute directs that Wal-Mart will not knowingly receive or accept any reduction in the premium shown on the policy unless there is a filing authorizing such reduction. For the reasons already stated, the court believes that Sooter was knowledgeable in insurance matters, and certainly his consultants were. The court does not believe that Wal-Mart, through its employees and consultants, can close their eyes and ears, as did the "three wise monkeys" in ancient Japan and say "we hear no evil, see no evil, and speak no evil." For the reasons already stated, the court is convinced that Wal-Mart and its consultants knew that this deal was too good to be true, and it cannot now say that it did not "knowingly" accept a reduction in premium that was not authorized by law.

Every state in which Wal-Mart had workers covered by the relevant policies has statutes similar to Ark.Stat. Ann. § 66-3019.[3]

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3. See Ala.Code § 27-12-14 (1975); Ariz.Rev.Stat.Ann. § 20-449 (1975); Fla.Stat.Ann. § 626.954(1)(n) (West Supp.1987); Ga. Code Ann. § 33-9-36 (1982); Ill.Ann.Stat. ch. 73, ¶ 763 (1965); Ind.Code Ann. § 27-1-20-30 (Burns 1986); Iowa Code Ann. § 507B.4 (Supp.1987); Kan.Stat.Ann. § 40-941 (1986); Ky.Rev. Stat. Ann. § 304.12-090 (1980); La.Rev.Stat.Ann. § 22-1214 (West 1978); Miss.Code Ann. § 83-3-121 (1972); Mo.Rev.Stat. § 379.356 (Supp. 1986); Neb.Rev.Stat. § 44-361 (1984); N.M. Stat.Ann. § 59A-16-15 (1978); N.C.Gen.Stat. § 58-44.5 (1982); Okla.Stat.Ann. tit. 36, § 1204 (1976); S.C.Code Ann. § 38-55-130 (Law.Co-op 1984); Tenn.Code Ann. § 56-8-104(8) (1980); Tex.Ins.Code Ann. § 21.21 § 4(8) (Vernon 1981).

In their briefs, the attorneys for the parties have very well set forth their views on whether the "deal" was legal or illegal and, if illegal, what should flow therefrom. Not surprisingly, Wal-Mart contends that, in the first place, the "deal" was legal, but if it was not, then the court should walk away from this matter, leaving the parties where it found them. On the other hand, Transit contends that only the "deal" was illegal, and that it clearly was, but that the court should still enforce the policies as issued and require the premiums which are set forth in the policies to be paid.

The court believes that it is necessary that the premiums be paid, and it is not certain that it must get into the "thicket" which conflicting authorities have created in relation to illegal contracts. In our case, Wal-Mart received exactly the coverage required by Arkansas and apparently the other states. Thus, the coverage complied with the various statutes. The policies, as issued, said that specified rates would be paid for this insurance. The premiums so calculated would seem to comply with the law of Arkansas and every other relevant state and, unless criteria not present in this case are present, the law of those states requires that the premium set forth on the policy be paid. Thus, it would not appear to be necessary to determine whether the "side agreement" was legal or illegal. The law provides the coverage to be maintained and the price that is to be charged and paid for it. In view of this, the court believes that Wal-Mart is required to pay the premiums called for in the insurance policies issued. The law requires that.

Wal-Mart, during the trial, and in its briefs filed in its behalf by its attorneys, has indicated that that would

not be "fair" because that is not what they contracted for. Yet, they have failed to show what they could have obtained the required insurance for from another provider, and this certainly should have been relevant, at least in relation to the third-party complaint which Wal-Mart filed against Alexander & Alexander. The court believes that it did not make this proof because there is none available which would indicate that any insurer anywhere in the country would have provided Wal-Mart with workers' compensation coverage which even came close to Miro's "deal." The court simply does not believe that any competent insurer would knowingly agree to provide Wal-Mart, or any other employer, with insurance covering employees in which there is a guaranteed cap on the premium to be charged. As in this case, this leaves the insurer in an unbelievably untenable position. Such an agreement could cause him to "go broke" as Transit did. In this case, the Receiver for Transit claims that over $21,000,000 in claims have been paid, and that before incurred but not reported claims have been identified and paid, they expect that total claim payments will exceed $30,000,000. Wal-Mart disagrees with this, but Sooter admitted during his testimony that he believes claims of 16 to 17 million dollars had been paid. It is certainly difficult to believe that any competent insurer would take on such an obligation, with no control over the results, nor would any reasonable employer believe that one would. It should be remembered that Transit, nor, in fact, Miro, A & A, or any other party except Wal-Mart, had nothing to do with the atrocious loss history that Wal-Mart had. That was something in the control of none of the participants other than Wal-Mart. What occurred is a perfect example of why the law of every state, and any reasonable

insurer, requires that loss history have some effect on the premiums to be paid.

Thus, for these reasons, the court is convinced that the law of every state requires that Wal-Mart pay the insurance premiums called for in the policies of insurance issued, and it is not necessary to determine whether the side agreement, or the entire agreement, was legal or illegal.

Be that as it may, if it is necessary to make such a determination, the court is convinced, for the reasons already set forth, that the side agreement was unenforceable and void. *See American Mutual Liability Ins. Co. v. Plywoods-Plastics Corp.*, 81 F.Supp. 157 (E.D.S.C.1948); *Key System Transit Lines v. Pacific Employers Ins. Co.*, 52 Cal.2d 800, 345 P.2d 257 (1959); *Contractor's Safety Assoc. v. California Comp. Ins. Co.*, 48 Cal.2d 71, 307 P.2d 626 (1957); *Warm Springs Forest Products Ind. v. Employee Benefits Ins. Co.*, 74 Or.App. 422, 703 P.2d 1008 (1985), *aff'd*, 300 Or. 617, 716 P.2d 740 (1986); *Mountain Fir Lbr. Co. v. E.B.I. Co.*, 296 Or. 639, 679 P.2d 296 (1984); *Biggs v. Reliance Life Ins. Co.*, 137 Tenn. 598, 195 S.W. 174 (Tenn.1917); *Associated Employers Lloyds v. Dillingham*, 262 S.W.2d 544 (Tex.Civ.App. 1953); *Glenn H. McCarthy, Inc. v. Knox*, 186 S.W.2d 832 (Tex.Civ.App. 1945).

In this respect, Wal-Mart earnestly contends in its briefs that the Arkansas case of *Pyramid Life Ins. Co. v. Patten*, 194 Ark. 987, 110 S.W.2d 526 (1937), is on point and represents not only the Arkansas rule, but the prevailing view. The court is convinced that a mere reading of that case shows that it is not, in fact, on point and is not,

in fact, controlling to the least degree. The court was applying a 1937 statute that is not even similar in most respects to the one applicable to this case. At 194 Ark. 989, 110 S.W.2d 526, the court said:

> The statute, *supra*, does not appear to be aimed at those receiving life insurance policies, but rather against companies and their agents. It does not prohibit any person from receiving a rebate, and it does not declare any policy to be void where a rebate is given or accepted. It does prescribe the penalty for the violation of the law, and under ordinary rules of construction, such penalty is exclusive. To give to the statute the effect contended for by appellant would be to enable it to take advantage of its own wrong. . . . Unless a statute probihits the insured from receiving a rebate and denounces a penalty for its violation, it clearly appears that such statute is designed to regulate insurance companies and not to punish the public who deals with them. In the statute under consideration, no reference is made to the insured, no provision is made for avoiding the policy, and it is clearly not the legislative intent that violations of the rebate law do more than inflict the punishment named therein.

The statutory scheme discussed in the *Patten* case is clearly different from the plan now in existence in Arkansas. Now, as discussed above, the law of Arkansas provides how premiums are to be calculated and does not allow rates or formulas for rates to be used that have not received prior approval from the Insurance Commissioner. In addition, as the court in *Patten* pointed out, there was then no statute that even, to the slightest degree, seemed to apply to the insured. That is no longer the case. Now, as discussed above, Arkansas law directs that no

insurer knowingly receive any premium other than one properly approved and shown on the policy.

In fact, not only is the *Patten* case not on point, there is other Arkansas authority which holds that an agreement which violates an anti-rebate statute similar to the one now in existence in Arkansas is unenforceable. In *Schneider v. O'Neal,* 145 F.Supp. 120 (E.D.Ark.1956), *aff'd in part and rev'd in part,* 243 F.2d 914 (8th Cir. 1957), Judge Trimble held that an agreement to give a rebate to a car dealer on insurance provided to the dealer in violation of the Arkansas rebate statute then in existence, and similar to the present one, is unenforceable.

VI. Doctrines of Waiver, Estoppel, and In Pari Delicto.

Wal-Mart contends that the Receiver should not recover because Transit has waived its right to do so, or is estopped from doing so. Based on the facts which the court believes exist in this case, as outlined in detail above, the court simply does not believe that the evidence supports the tests laid down for estoppel in cases such as *Askew Trust v. Hopkins,* 15 Ark. App. 19, 688 S.W.2d 316 (1985). In Arkansas, waived is used interchangeably with estoppel, and for a waiver to be binding it must operate by way of estoppel. *Continental Ins. Co. v. Stanley,* 263 Ark. 638, 569 S.W.2d 653 (1978). The evidence simply does not support a finding that Transit or the Receiver knowingly waived any right granted to it by the insurance policies or is estopped from exercising those rights.

Wal-Mart also contends that the court should apply the doctrine of *pari delicto* and leave the parties where it

finds them. According to this doctrine, in a case where the court finds that the parties are *in pari delicto,* it will not allow itself to be made the instrument of enforcing obligations arising out of an agreement which is illegal. *Wommack v. Maner,* 227 Ark. 786, 301 S.W.2d 438 (1957); 17 Am.Jur.2d *Contracts* § 216. The obvious purpose of the rule is to discourage illegal agreements and it extends to any agreement which is illegal, immoral, against public policy, or prohibited by statute. *Ganntt v. Ark. P. & L. Co.,* 189 Ark. 449, 74 S.W.2d 232 (1934); *Tate v. Gould,* 175 Ark. 306, 299 S.W. 24 (1927).

Because of the reasons for the rule, the court is convinced that it should not be applied in a case such as this one. To apply the rule in this case would not further the public interest and would not discourage illegal, immoral, and against public policy contracts. Instead, it would encourage them and allow Wal-Mart to walk away from this matter after having received 15 to 30 million dollars in benefits after paying premiums that are a fraction of that. As indicated, the "deal" which Wal-Mart received in this case was not in compliance with the law of any state, and Wal-Mart and its consultants didn't believe that it was. Why then should the court apply a rule that has salutary purposes in such a way as to fly directly in the face of the laudable reasons for the rule?

Other courts have held that estoppel, waiver, mistake or other affirmative defenses of that nature are not available in workers' compensation cases brought to recover premiums based on rates promulgated and on file with the applicable insurance department. *See Walker v. Bituminous Casualty Corp.,* 74 Ga.App. 517, 40 S.E.2d 228

(1946); *Travelers Indemnity Company v. Collier,* 205 Okl. 247, 237 P.2d 153 (Okla.1951); *Silver Threads, Inc. v. Insurance Company of North America,* 530 S.W.2d 874 (Tex.Civ.App.1975); *Associated Employers Lloyds v. Dillingham,* 262 S.W.2d 544 (Tex.Civ.App.1953); *Traders and General Ins. Co. v. Frozen Food Express,* 255 S.W.2d 378 (Tex.Civ.App.1953); *Brown and Root v. Traders and General Ins. Co.,* 135 S.W.2d 534 (Tex.Civ.App.1939).

In any event, the court is convinced that this is not a case in which Transit is attempting to enforce an illegal agreement. Instead, Wal-Mart is. Wal-Mart brought this lawsuit asking the court to enforce the "side agreement." If it is not enforced by the court, Wal-Mart is bound by the policies issued and accepted which require payment of additional premiums. As indicated above, there is a line of cases that hold that the court should not allow or consider parol evidence to show what the "deal" was when its purpose was illegal or made to deceive and mislead public authorities. *See* cases cited at page 39 of this opinion. If Wal-Mart is permitted to avoid its obligation to pay workers' compensation premiums according to state rates for the very substantial benefits that it received, it has successfully enforced an illegal contract made to deceive public authorities and has frustrated the purpose of premium regulations.

On the other hand, Transit does not seek to enforce an illegal contract. Its counterclaim is based on the policies which were issued, delivered and accepted by Wal-Mart. The policies are standard workers' compensation policies with premiums based on estimated payrolls, state rates, and experience modifiers promulgated as contem-

plated by the law of each of the states in which the policies were to apply. The policy form was approved and on file with the Arkansas Insurance Department at least as 1980 and contained the standard formula used throughout the country to determine the premium to be charged. The policies are completely separate and independent from the "side agreement" and the Receiver requires no aid nor reference to such illegal agreement in calculating the additional premiums owed. Thus, requiring Wal-Mart to pay the premiums called for in the valid policy is not an enforcement of an illegal contract, and in doing so, the court is only doing what the law of Arkansas and every other relevant jurisdiction requires.

For these reasons, the court finds it unnecessary to discuss the very complicated area of the law relative to whether a trustee or receiver may be prevented from enforcing a contract provision because of the acts of the bankrupt prior to the insolvency.

VII. Tail Coverage

The court has been asked by Transit to declare the tail coverage to be null and void because of misrepresentations made by and in behalf of Wal-Mart. The court finds that the evidence adduced at the trial simply does not support this. Unlike the workers' compensation insurance policies, the court can find no provision of law which does not permit that type of insurance. Apparently, the law allows anyone to insure about anything that they can find an insurance carrier to insure. If news media reports are accurate, that ranges from parts of a woman's anatomy to whether it will rain at a particular sporting event. The court can find no basis to hold that the tail coverage was

not in compliance with law, and the evidence simply does not support a finding that Wal-Mart or its agents misrepresented the facts resulting in the incredibly bad deal that Miro made in behalf of Transit. Instead, the evidence is that the claims files in the Alexsis office were offered to Miro, but that he declined to consider them. Incredibly, he decided that, because he was familiar with Alexsis, he would accept reserves established by its employees and would charge nothing for incurred but not reported claims, apparently because he was going to invest the premiums received in "Euro Dollars," whatever that means.

In this respect, it is appropriate for the court to say that the evidence reflects that there is more than enough fault to go around in this case. Transit and its managing agent, Muldoon, were guilty of very ample malfeasances. They loosed this disaster (Miro) waiting to happen on the public and on themselves with almost no control of it. The court has not ruled as it has because it finds the employees of Transit or Muldoon blameless by any means. Instead, the court is convinced that, for the reasons discussed, the law and public policy demand that Wal-Mart pay an adequate premium for the insurance it received and that it not be allowed to use its tremendous influence and bargaining power to require other employers or other members of the public to pay millions of dollars for claims paid to its injured employees.

The court finds the tail coverage to have been properly issued within the actual or apparent authority of Miro, and that policy is enforceable according to its terms.

VIII. Third Party Complaint Against Alexander & Alexander

Wal-Mart brought Alexander & Alexander into this lawsuit, asking that, in the event that judgment was rendered against it, Alexander & Alexander be ordered to reimburse it. The court finds, without question, that Wal-Mart's consultant did not serve it well. There is little question that Stanley and Hallinan, with a combined experience in the insurance business of over sixty years, should have known that this "deal" was too good to be true, and that it did not comply with the law of any jurisdiction. The court is convinced that, in fact, they did know that. For whatever reason, they did not, according to the evidence, advise Wal-Mart of this, and they are unquestionably derelict in their duties in not doing so.

After having said that, the court frankly doesn't know what it can do about it. What are Wal-Mart's damages? In the court's view, they were not proved at the trial. For the reasons indicated, the court is convinced that Wal-Mart is being required to pay for the coverage what the law requires it to pay. There was no evidence which indicates that, if Wal-Mart had been properly advised by Hallinan and Stanley, it could have gotten like coverage for some specified amount. As indicated, the court is overwhelmingly convinced that no other sane insurer would make the deal that Miro made. For this reason, there is no basis for the court to determine that Alexander & Alexander owes to Wal-Mart the difference between the premiums that it will be required to pay according to the policy, and the $3.5 million which Miro agreed to accept.

Likewise, there is no evidence from which the court could find that Wal-Mart could have received the same coverage for anything less than the amount that it is required to pay as a result of this lawsuit. It is true that some of Wal-Mart's witnesses testified that they believed that deals calling for premiums less than the manual rates could have been obtained, but there was no evidence from which the court can find that that is true nor certainly any evidence which indicates, even if true, what that coverage would have cost.

Since this is true, there is absolutely no basis for this court to award a judgment in favor of Wal-Mart against A & A on any basis other than pure speculation. The law simply does not allow that.

IX. Conclusion and Judgment

For the reasons set forth above, the court finds that Wal-Mart should be required to pay the premiums called for in the two workers' compensation policies of insurance discussed in detail above. Randy Watkins testified at the trial and submitted defendant's exhibit 40 as a summary of premium calculations which he made. The calculations, according to his testimony, were based on audits performed by White & White and John Sooter and rates contained in the 1983-84 NCCI manual. He reviewed Transit's filings for all applicable jurisdictions and applied appropriate deviations, experience modifiers and discounts, and computed the premium according to standard underwriting guidelines.

While Wal-Mart contends in its brief that his testimony was not adequate on damages, they failed to refute

it during the trial to any degree, and did not offer evidence of their own. For this reason, the court believes that Mr. Watkins' testimony does correctly set forth the premiums that are due on the policies in question for the coverage provided.

Exhibit 40 contains two separate calculations for the premium for the policy year 1983-84. The reason for this undoubtedly was that, as the court recalls, while Wal-Mart's attorney did not object to the introduction of the first White & White audit, he contended that the payroll information was not correct. For this reason, Watkins also calculated the premiums for that year based upon what John Sooter said the payrolls were. There is a difference of in excess of $2,000,000 caused by this. However, because Wal-Mart's attorneys did not stipulate that the figures in the first audit were accurate, and because the White & White auditors were not called to testify, those figures, in the court's view, would be "hearsay." For this reason, the court will accept the premium determined on the basis of Sooter's estimate of the payroll for the first policy year.

This means that Wal-Mart owes total premiums for two years in the amount of $16,772,144.00. Such judgment will bear prejudgment interest from the date on which it was possible to calculate the premiums due. *See Bank of Mulberry v. Fireman's Fund Ins. Co.,* 720 F.2d 501 (8th Cir.1983), and cases cited in that decision.

Because the Receiver is in a better position than the court to determine on what date pre-judgment interest should commence, and because of the matter of certain funds being paid into the registry of the court, the court

directs that Receiver's counsel prepare and forward to the court, within ten (10) days of the receipt of this opinion, a judgment in compliance with the court's decision. In respect to the prejudgment interest issue, the court directs that the Receiver cite the court to the evidence in the record which establishes the date on which such interest should commence.

(2)

No. 88-1275

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

October Term, 1988

LEWIS R. CRIST,
RECEIVER FOR TRANSIT CASUALTY COMPANY,
Petitioner,

vs.

WAL-MART STORES, INC. AND
ALEXANDER AND ALEXANDER, INC.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

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QUESTION PRESENTED

Whether the Court of Appeals correctly determined that, under Arkansas state law, where insurance policies are declared illegal due to the way the policies were structured by the insurance company, the receiver for the insolvent insurance company was barred from recovery by the common law doctrine of in pari delicto on a claim against its insured for additional premiums which were not part of the agreement between the parties.

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LEWIS R. CRIST,
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ON PETITION FOR A WRIT OF CERTIORARI
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Brief In Opposition Of Respondent Wal-Mart Stores, Inc.

STATUTES INVOLVED

Although the Petitioner cites a number of statutes dealing with workers compensation insurance in various states, none of these statutes is relevant to the issues presented in the Petition for a Writ of Certiorari. Petitioner apparently attempts to create at least an illusion that the laws from numerous states are in controversy here. In fact, however, only the state common law of Arkansas, which the Eighth

Circuit properly applied to those holdings challenged by petitioner Crist, is involved. Respondent Wal-Mart Stores, Inc. ("Wal-Mart")[1] objects, therefore, to Petitioner's inclusion of a vast number of statutes which have no bearing on this Court's consideration of the Petition.

STATEMENT OF THE CASE

This action was brought in federal court by virtue of the diversity of citizenship of the parties involved. It concerns only issues of state law and policy.

In 1983, respondent Wal-Mart, headquartered in Bentonville, Arkansas, sought bids for obtaining compensation insurance coverage for its workers. (Pet. App. 4a). Offers were solicited through Wal-Mart's insurance consultant, Alexander & Alexander, Inc. ("A & A"). (*Id.*). One of the quotes submitted to Wal-Mart came from Transit Casualty Company ("Transit"), which is now represented in this litigation by its receiver, petitioner Lewis R. Crist. Transit offered to supply Wal-Mart's workers compensation insurance coverage for the coming 1983-1984 year for a total premium of $3.5 million. Wal-Mart accepted this bid. (Pet. App. 5a-6a).

As part of the bid process, Wal-Mart had supplied Transit with its projected payroll for workers for the coming year. Transit was to use this projected payroll in the issued policy. Transit had the responsibility for structuring the issued workers compensation policy, with this payroll, to comply with both the parties' premium agreement and Transit's own

[1]Pursuant to Supreme Court Rule 28.1, Wal-Mart Stores, Inc. informs the Court that it has no parent corporation and no subsidiaries other than wholly-owned subsidiaries. As to affiliates, it is in partnership with Cullum Companies, Inc. in Hypermart ☆ USA, a Texas general partnership.

insurance rate filings approved by the various states in which Wal-Mart had employees. (*See* Pet. App. 11a-15a). Wal-Mart reasonably expected that Transit would be able to issue a legitimate policy containing a $3.5 million premium cap. As the Eighth Circuit observed, "while a $3.5 million guaranteed premium was certainly a competitive offer, it was by no means unreasonably low in comparison to Wal-Mart's demonstrated loss history at the time." (Pet. App. 12a). To provide the coverage for $3.5 million, Transit would only need to use some of the many mechanisms, which are outlined in the Court of Appeals' decision, "by which filed workers' compensation rates could be legitimately adjusted to achieve a quoted premium." (Pet. App. 14a). As noted by the Eighth Circuit, "[d]evices such as premium discounts, retrospective rating, policy dividends, rate deviations and scheduled rating were available to legally reduce premium charges below what would have to be paid pursuant to filed rates." (*Id.*).

When Transit applied existing rates to Wal-Mart's estimated payroll, it obtained a premium price higher than $3.5 million. (Pet. App. 6a-7a). Rather than using available premium discounts or approved deviations to reduce this premium, however, Transit simply took the shortcut of depressing Wal-Mart's payroll as reported in the policy to artificially achieve the $3.5 million premium. (*Id.*). Transit sent the policy to Wal-Mart's insurance broker, A & A, who reviewed the policy and sent it to Wal-Mart. When Wal-Mart noted and questioned the reduced payroll in the policy, A & A assured it that Transit's procedure was common and appropriate.

In 1984, Transit again offered Wal-Mart coverage for the coming year at a guaranteed $3.5 million premium.

(*See* Pet. App. 7a). Again, Transit had the responsibility to structure a legitimate policy which complied with the parties' agreement. Again, however, Transit did not use any of the available mechanisms to validly obtain the $3.5 million cap. Instead, Transit took the shortcut of depressing Wal-Mart's estimated payroll to reach the $3.5 million premium. (*See* Pet. App. 7a).

Near the end of this second policy year, trouble arose between Transit and the reinsurers with which it had placed Wal-Mart's policy risk. (Pet. App. 7a-8a). As a result, these reinsurers stopped paying claims made against the Wal-Mart policies. (*Id.*). At that time, Transit suddenly was no longer satisfied with receiving only $3.5 million per year in premium. Instead, Transit unilaterally replaced the depressed payroll figure in the policies with the estimated payroll that Wal-Mart had given it earlier. Because of the filed rates for which Transit had not obtained deviations, this resulted in policies showing a higher premium. Even though it was Transit who had included the lower payroll as a shortcut in the first place to cover its failure to obtain the needed deviations and premium reductions, Transit now demanded that Wal-Mart pay the additional premium indicated in the revised policies. (*Id.*).

Wal-Mart refused to accede to Transit's demands for higher premiums than those agreed, and initiated a declaratory judgment action against Transit in the United States District Court for the Western District of Arkansas, seeking to enforce the $3.5 million premium agreements for the 1983-1984 and 1984-1985 policy years. Transit counterclaimed for over $18,000,000 in additional premiums that it claimed Wal-Mart owed. Wal-Mart initiated a third-party action against A & A for indemnity on Transit's counterclaim.

Prior to completion of the litigation, Transit was declared insolvent and petitioner Crist was appointed as receiver to continue the litigation on behalf of Transit. After a seven day trial, the matter was submitted to the district court, with all parties agreeing that the common law issues were governed by Arkansas law. The district court held that the policies proposed and submitted by Transit with the depressed payrolls violated the statutory law of the relevant states. (Pet. App. 71a-85a). The district court permitted Transit's receiver to escape the impact of this illegality, however, by concluding that Transit's agent, who had negotiated the agreement and structured the policies, did not have actual or apparent authority under Arkansas law to enter into the agreement with Wal-Mart in the first place. (Pet. App. 63a-71a). The district court further rejected Wal-Mart's argument that Transit's receiver, petitioner Crist, should not be permitted to benefit from Transit's wrongdoing by finding the Arkansas law of in pari delicto inapplicable. (Pet. App. 85a-88a). Accordingly, the district court allowed Crist to recover the additional premiums under the insurance policies and entered judgment for Crist for approximately $16 million, plus interest.

Wal-Mart appealed the district court's judgment to the United States Court of Appeals for the Eighth Circuit, which reversed after a lengthy analysis of the governing law of Arkansas. In its opinion, the Court of Appeals acknowledged the district court's holding that the insurance policies as issued by Transit violated the statutory laws of the relevant states. (Pet. App. 15a-18a). The Eighth Circuit also held, however, that Transit's agent did have apparent authority, under Arkansas common law, to make the premium agreement with Wal-Mart and issue the policies. (Pet.

App. 9a-15a). Echoing the district court's finding that there was "more than enough fault to go around in this case," (Pet. App. 20a), the Court of Appeals concluded that, under Arkansas law, Crist was barred by the doctrine of in pari delicto from benefiting from the wrongdoing of the party it represented. (Pet. App. 18a-22a). The Court of Appeals held that the policies could not be enforced, therefore, even if the correct payrolls were substituted.[2] It concluded that application of the doctrine of in pari delicto not only was required by Arkansas law, but also furthered the public policy underlying workers compensation insurance. (Pet. App. 22a).

REASONS FOR DENYING THE WRIT

Crist's Petition for a Writ of Certiorari should be denied because the challenged decision of the Court of Appeals involves solely a question of Arkansas state law. Further, the Eighth Circuit properly interpreted and applied the law of Arkansas in this case. The law of Arkansas provides that Transit's receiver is barred from recovering damages from Wal-Mart by the doctrine of in pari delicto. Arkansas does not permit Crist to escape responsibility for the actions of Transit merely because of his receiver status. Finally, the Petition should be denied because, despite Crist's protestations to the contrary, no national interests are involved

[2]Crist erroneously asserts in his Petition that two agreements existed between the parties—an unenforceable premium "side agreement" and the "enforceable" policies. As the Court of Appeals observed, however, only one contract existed between the parties: for insurance coverage at a $3.5 million premium. In light of the manner in which the policies were ultimately structured by Transit, the entire contract between the parties was unenforceable under Arkansas law, which prohibited the severance of the one contract into two separate agreements. (*See* Pet. App. at 18a-19a). Crist fails to inform this Court that the "separate agreement" issue was decided against him by the Court of Appeals, and that it was so decided solely as a matter of Arkansas law.

in this case, which concerns a unique fact situation decided under Arkansas law.

I.

This Case Presents Only Issues Of State Law

Petitioner Crist challenges only the Eighth Circuit's holding that he was barred from recovering damages by the doctrine of in pari delicto. In his discussion of this challenge, however, Crist never reveals the most important aspect of the Eighth Circuit's holding: the Eighth Circuit's decision to bar Transit's receiver from recovering damages was based solely on the state law of Arkansas.

The parties in this action agreed, at all times, that the common law matters were to be governed by the law of Arkansas, where Wal-Mart is headquartered and where the action was maintained in district court. Thus, the district court applied Arkansas law in analyzing the issue of in pari delicto, (Pet. App. 85a-88a), as did the Eighth Circuit. (Pet. App. 19a-22a). The Eighth Circuit held that, under Arkansas common law, petitioner Crist, acting as Transit's receiver, could not recover from Wal-Mart when Transit was the party that structured the illegal policies. (Pet. App. 20a).

Even though Crist disputes in his Petition only this portion of the Eighth Circuit's decision, Crist disingenuously avoids mentioning that the disputed issue was governed by and decided solely under Arkansas law. This Court does not review, as a general matter, issues decided by intermediate courts of appeals solely on state law grounds. Indeed, at one time, Rule 19 of this Court provided that the Court would consider review of a decision of a court of appeals that resolved "an important state or territorial question in a way in conflict with applicable state or territorial

law." Sup. Ct. R. 19, 398 U.S. 1009, 1030-31 (1970). In its current Rule 17, however, this Court has excluded this category from those which it considers to present special and important reasons for review by writ of certiorari. *See* Sup. Ct. R. 17.

The Eighth Circuit's interpretation of the Arkansas law of in pari delicto certainly presents no special basis for this Court's departure from its normal reluctance to interfere with the interpretation of state law by federal appellate courts. *See, e.g., Huddleston v. Dwyer,* 322 U.S. 232, 237 (1944). Although Crist attempts to argue that the Arkansas law applied by the Court of Appeals conflicts with that applied in other jurisdictions, conflict among courts on questions of state law is not a reason for this Court to grant a writ of certiorari. *See Ruhlin v. New York Life Ins. Co.,* 304 U.S. 202, 206 (1938) ("As to questions controlled by state law, however, conflict among circuits is not of itself a reason for granting a writ of certiorari. The conflict may be merely corollary to a permissible difference of opinion in the state courts.").

Further, although Crist notes several times his disagreement with the Eighth Circuit's analysis of the facts, this Court "do[es] not grant a certiorari to review evidence and discuss specific facts." *United States v. Johnston,* 268 U.S. 220, 227 (1925). At best, Crist raises issues of state law and policy. As this Court noted in *Huddleston v. Dwyer,* 322 U.S. 232, 237 (1944), however, "ordinarily we accept and therefore do not review, save in exceptional cases, the considered determination of questions of state law by the intermediate federal appellate courts." *Accord Butner v.*

United States, 440 U.S. 48, 51, 57-58 (1979).[3] Crist raises no issues worthy of this Court's grant of review.

II.

The Eighth Circuit's Decision Is Consistent With Arkansas Law

Not only does petitioner Crist fail to reveal that the Eighth Circuit's decision rests on Arkansas law, he completely fails even to suggest that the Eighth Circuit's decision incorrectly interpreted Arkansas law on in pari delicto. This failure is understandable, because the Eighth Circuit's interpretation and application of the law of in pari delicto is fully consistent with the law of Arkansas.[4]

A. The Eighth Circuit Properly Held That Arkansas Law Required Application Of The Doctrine Of In Pari Delicto

As the Eighth Circuit concluded, "Arkansas has recognized and applied the doctrine of in pari delicto when parties to an illegal contract are equally culpable." (Pet. App. 19a). The Arkansas courts have held that no relief shall be granted to a party, such as Transit here, when that party was equally cognizant of the illegality of the contract. *See*

---

[3]In *Butner*, this Court declined to review an issue on which the court of appeals had reversed the district court on a matter of state law, even though the Court was reviewing other aspects of the court of appeals' decision. This Court stated that it "did not grant certiorari to decide whether the Court of Appeals correctly applied North Carolina law," and "decline[d] to review the state-law question," even though the parties argued the issue "at great length." 440 U.S. at 51, 57-58.

[4]As noted above, previous Sup. Ct. R. 19 required that, at a minimum, the state law question be decided "in a way in conflict with applicable state . . . law" before this Court would consider granting review. Thus, even under the formulation which this Court has since discarded, Crist has failed to raise a question worthy of review because he does not — and cannot — show that the Eighth Circuit's decision is in conflict with the controlling Arkansas precedent.

Long v. Mabry, 250 Ark. 947, 470 S.W.2d 319, 321 (1971); *Womack v. Maner*, 227 Ark. 786, 301 S.W.2d 438, 439 (1957); *City Nat'l Bank v. First Nat'l Bank & Trust Co.*, 22 Ark. App. 5, 732 S.W.2d 489, 495-96 (1987); *see also Williams v. Wilson*, 181 F.Supp. 351, 354 (E.D. Ark. 1960).

Based on this undisputed Arkansas law, the Eighth Circuit correctly concluded that Transit's receiver could not recover from Wal-Mart where Transit had been the architect of the illegal policies. (*See* Pet. App. 18a-22a). It was Transit who had the responsibility to structure the premium agreement properly; it was Transit who failed to seek the necessary premium reductions; it was Transit who instead issued the policies containing the depressed payrolls; and it was Transit, and ultimately its receiver, who sought to profit from its illegal actions by demanding additional premiums from Wal-Mart. Agreeing with the district court that "there is more than enough fault to go around in this case," the Eighth Circuit properly held that Arkansas law barred Transit's receiver from reaping the profits of Transit's wrongdoing. (Pet. App. 20a).

Transit's receiver challenges the Eighth Circuit's application of the doctrine of in pari delicto, not by citing relevant Arkansas law, but by arguing that "public policy" requires that the insurance policies alone should somehow be enforced without regard to their illegality or the rest of the agreement between the parties. Quite contrary to the receiver's allegations, however, the Court of Appeals carefully considered the state law governing workers compensation insurance and determined that the goal of these laws would best be served by applying the doctrine of in pari delicto. Insurance regulations are aimed principally at regu-

lating the conduct of the insurers, not the insured. It is the insurance companies that have the greatest control over insurance policies and premiums and that have the greatest ability to cause harm when they fail to conform their insurance policies to the law in accordance with the legitimate expectations of insureds.

Here, the harm suffered came at the hands of Transit, the insurance company. The Court of Appeals properly held that, under the circumstances of this case, the public good was best served by holding the receiver to the consequences of Transit's acts. As the Court of Appeals noted:

> [W]e believe . . . that application of the doctrine [of in pari delicto] here would work to discourage insurers from permitting agents to quote premiums and structure policies in violation of state insurance regulations. Requiring the payment of greater premiums by Wal-Mart not only stands in direct conflict with the terms of the original agreement as the parties expected it to be carried out, but operates to reward Transit for structuring an illegal arrangement which it, as the insurer, was in the best position to prevent.

(Pet. App. 22a).

As the Eighth Circuit concluded, Arkansas law holds Transit's receiver to the consequences of Transit's bad acts. Far from undercutting the policy underlying workers compensation insurance laws, as the receiver suggests, the Eighth Circuit's holding is essential to carry out that policy. The public interest in controlling insurers requires that Transit and its receiver bear their share of the consequences of Transit's actions. Transit had the responsibility to issue policies that complied with the laws of the various states. Transit never made the effort. The supposed "public policy"

advanced by Transit's receiver would reward Transit and other insurers for inducing insureds to accept insurance based on premiums that the insurance companies never intended to justify. The Court of Appeals correctly identified and applied the controlling law and policy.

B. Arkansas Law Does Not Permit Crist To Hide Behind His Receiver Status To Avoid Application Of The Doctrine Of In Pari Delicto

In his Petition for a Writ of Certiorari, Crist argues that the Eighth Circuit's rejection of his novel "shield" defense is contrary to the best interests of the public and ignores decisions from other jurisdictions which are on point. As already discussed, however, Crist does not and cannot argue that the decision of the Eighth Circuit is contrary to the law of Arkansas. Indeed, the existing Arkansas precedent rejects Crist's attempt to immunize himself from the acts of Transit.

Arkansas law provides that receivers are bound by the acts of the insolvent corporation in actions by or on behalf of the corporation. For example, in *Schneider v. O'Neal*, 145 F.Supp. 120 (E.D. Ark. 1956), *aff'd in relevant part*, 243 F.2d 914 (8th Cir. 1957), the district court for the Eastern District of Arkansas held that, under Arkansas law, a trustee asserting the rights of a bankrupt is responsible for the bad acts of the bankrupt. The district court applied, therefore, the doctrine of in pari delicto to bar the trustee from recovering damages.

On appeal from the district court's decision in *Schneider*, the Eighth Circuit affirmed the district court's holding that a trustee in bankruptcy is accountable for the acts of the bankrupt when the trustee is asserting the bankrupt's rights. The Court of Appeals reversed only the district court's find-

ing that the trustee had waived his ability to also assert the independent rights of the creditors — as opposed to the rights of the bankrupt — under Section 70(e) of the Bankruptcy Act. As the Eighth Circuit noted, the trustee would not be bound by the bankrupt's bad acts when the trustee is asserting only rights which the creditors have independent of the bankrupt. *See Schneider v. O'Neal*, 243 F.2d 914 (8th Cir. 1957).

Here, Crist represented the interests of Transit in pursuing this litigation and is bound by Transit's bad acts. Transit began the litigation and conducted much of the discovery. Crist only carried on the litigation in place of Transit after Transit was placed in receivership. Crist does not argue that he represents any rights that creditors of Transit themselves have against Wal-Mart independent of the rights of Transit. Indeed, it would be hard to envision any claim that the creditors of Transit could have against Wal-Mart, apart from the contract claim of Transit.

Crist did not and could not maintain this action for recovery of additional premiums on behalf of the creditors, as he asserts in his Petition. Indeed, it should be noted that the statute which Crist cites for the proposition that he represents the interests of creditors, Mo. Rev. Stat. § 375.-670, provides only that the receiver may administer demands by creditors on the insolvent's estate. It does not give the receiver the power to maintain actions against third parties in the name of the creditors. Thus, Crist is here merely continuing to assert the rights, if any, which Transit had when the litigation began. Any recovery it collected on Transit's behalf would have been added to the

estate, which must then be administered with the creditors in mind.

The Eighth Circuit correctly held, therefore, that, under Arkansas law, Crist must accept responsibility for the bad acts of the insurance company on whose behalf and in whose stead the litigation was conducted. Ignoring Arkansas law, however, Crist argues that the Court of Appeals should have immunized him from Transit's actions. Crist asserts that the Court of Appeals should have first extended the doctrine of *D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 315 U.S. 447 (1942), to the workers compensation insurance industry and then inserted it into Arkansas state law.[5] In *D'Oench*, this Court held that the Federal Deposit Insurance Corporation, which had acquired notes of an insolvent bank, would not be subject to the defenses against enforcement of the notes when the defenses did not appear in the bank's records. Crist argues that, just as defenses against enforcement of a note would not be valid against the FDIC, defenses against enforcement of the unlawful insurance policies should not be valid against Crist, acting as receiver for Transit.

Even ignoring the obvious flaws in Crist's argument, such as the fact that the *D'Oench* doctrine applies only to defenses that are hidden from the FDIC, and not to defenses which are plainly revealed by the documents held by the

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[5]Crist's standing to assert this argument in his Petition for Certiorari is questionable. Crist, acting as receiver for Transit and appellee in the action below, did not raise the *D'Oench* shield defense before the Eighth Circuit. Instead, Crist sought and, over objection, obtained leave to also submit a separate amicus brief in his capacity as director of the Missouri Department of Insurance. He addressed this shield defense only in this "amicus" capacity. As the appellee before the Court of Appeals, Crist did not even address the issue until his motion for rehearing and rehearing en banc following issuance of the Eighth Circuit's decision.

institution,[6] Crist simply fails to show any Arkansas authority for his assertion that *D'Oench* should be or would be first extended outside the law of negotiable instruments and then accepted into the law of Arkansas. Contrary to Crist's assertions, *D'Oench* has not been extended beyond financial institutions, and, indeed, some courts have questioned whether the FDIC itself can invoke the *D'Oench* doctrine, as codified in 12 U.S.C. § 1823(e), when the FDIC is acting as a receiver of a failed bank, rather than as a holder of notes as it was in *D'Oench*. *E.g.*, *Jones v. Federal Deposit Ins. Corp.*, 151 Ga. App. 619, 260 S.E.2d 751 (1979) (refusing to apply the codified version of the *D'Oench* doctrine to the FDIC acting as receiver); *see Federal Deposit Ins. Corp. v. Vogel*, 437 F.Supp. 660, 663 (E.D. Wisc. 1977).

Moreover, those cases in which the *D'Oench* doctrine has been extended to financial institutions other than the FDIC acting as a holder of a note have invariably involved the application of federal common law. *See Firstsouth, F.A. v. Aqua Const. Inc.*, 858 F.2d 441 (8th Cir. 1988) (extending the *D'Oench* doctrine to the Federal Savings and Loan Insurance Corporation under federal common law). The only case on which Crist relies to support his assertion that the policies underlying the *D'Oench* doctrine have "long been applied in the insurance industry" is from Texas

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[6]Here, for example, the premium agreement between Transit and Wal-Mart was reflected in a cover note and binder. (Pet. App. 6a). Crist's assertion that this was solely an "oral agreement" (Pet. App. 8) is false; the premium agreement was in writing and discoverable by the insurance regulators had they examined Transit's files.

— a jurisdiction whose law on this issue is not relevant here. (*See* Pet. App. 13).[7]

The Eighth Circuit held that Transit's receiver failed to persuade the court that the Arkansas courts would extend the *D'Oench* doctrine beyond the confines of the banking industry. (Pet. App. 21a, n.11). In the face of the flatly contrary precedent under Arkansas state law, the Eighth Circuit properly refused to extend the *D'Oench* doctrine to shield Crist from Transit's guilt.

III.

No National Concerns Are Raised By The Eighth Circuit's Application Of The Arkansas In Pari Delicto Doctrine

Throughout his Petition, Crist attempts to create the impression that the state law issues in this case are of national importance. He asserts that the Eighth Circuit's decision disrupts the "uniform" regulation of workers compensation insurance in the fifty states, leaves insurance regulators with no means of enforcing workers compensation regulations, and leaves Wal-Mart in a position of having "avoided paying its statutory premium," "avoided paying its injured workers," and "profiting at the expense of guarantee funds across the country."

Crist's hyperbolic allegations are not only groundless but are, indeed, directly contrary to the facts. Crist's repeated assertion that workers compensation insurance is

[7]Crist is apparently attempting to persuade this Court to review an alleged conflict between the law of different states, namely Arkansas and Texas, as to whether receivers of failed companies should be held responsible for the acts of the companies. This Court does not, of course, grant certiorari to resolve permissible differences of opinion among state courts, each interpreting its own state's laws. *See Ruhlin v. New York Life Ins. Co.*, 304 U.S. 202, 206 (1938).

uniformly regulated is contradicted by the regulations themselves. States vary greatly in the degree to which they regulate workers compensation insurance and, as noted by the Eighth Circuit, many states were moving towards deregulation of workers compensation insurance during the years that the policies were negotiated between Transit and Wal-Mart. (Pet. App. 14a, n.5).

The Eighth Circuit's decision does not disrupt the regulation of workers compensation insurance among the states, but in fact encourages adherence to the regulations by insurance companies. By prohibiting Transit's receiver from profiting from Transit's violation of the regulations, the Eighth Circuit sent the insurance industry a much needed warning that insurers cannot continue to promise insurance premiums they never intend to justify. As the Eighth Circuit concluded, "application of the doctrine here would work to discourage insurers from permitting agents to quote premiums and structure policies in violation of state insurance regulations." (Pet. App. 22a).

Crist's passionate argument that, as a result of the Eighth Circuit's holding, regulators have no means of enforcing their regulations, is also without basis. This case concerns only an interpretation of Arkansas law in a situation where a receiver, who also was an insurance regulator, continued to pursue an action on behalf of the insolvent insurance company against the insured. The ability of the insurance regulators to police the insurance industry itself remains unaffected by the Eighth Circuit's decision.

Finally, Crist's repeated accusations that Wal-Mart is somehow improperly benefiting from the Eighth Circuit's decision are both false and irresponsible. Wal-Mart paid $7 million to Transit for its two years of insurance coverage —

an amount which the Eighth Circuit noted was fair and reasonable at the time the premium agreement was reached. (*See* Pet. App. 11a-12a). Further, no injured worker has gone unpaid and Wal-Mart has not taken any advantage of state guarantee funds. These state guarantee funds are set up and funded by the insurance industry to provide for eventualities such as this — when an insurance company, like Transit, offers numerous insureds more than it can deliver.[8] Here, Transit promised Wal-Mart that it would provide Wal-Mart with needed insurance coverage for $3.5 million a year, but Transit did not deliver.

This case involves an isolated issue of Arkansas law applied to a unique set of facts. Transit's receiver cannot transform this issue into one of national significance by making unsupported assertions. Crist fails to raise any issue of merit in his Petition.

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[8]Crist's assertion that the state guarantee funds are harmed by the decision of the Eighth Circuit is more than slightly disingenuous in light of the fact that these same guarantee funds are now suing Wal-Mart across the country, in their own state courts under the different laws of each of their own states, seeking to recover amounts that the funds paid on Transit's behalf.

CONCLUSION

The Court of Appeals decided this case on a matter of Arkansas state law, in accord with Arkansas precedent. In his Petition, Transit's receiver Crist does not contend otherwise. The Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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Dated: February 27, 1989

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No. 88-1275

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

LEWIS R. CRIST, RECEIVER FOR TRANSIT CASUALTY COMPANY
Petitioner

v.

WAL-MART STORES, INC. AND
ALEXANDER AND ALEXANDER, INC.
Respondents

MOTION FOR LEAVE TO FILE AND AMICUS CURIAE BRIEF OF TEXAS PROPERTY AND CASUALTY INSURANCE GUARANTY ASSOCIATION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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The Texas Property and Casualty Insurance Guaranty Association hereby respectfully moves for leave to file the attached brief *amicus curiae* in this case. The consent of attorney for the Petitioner has been obtained. The consent of the attorney for the Respondent was requested but refused.

The interest of the Texas Property and Casualty Insurance Guaranty Association arises from the fact that it functions as a statutory association whose duty is to pay certain "covered claims" arising from insurance insolvencies. The instant case involves a finding of *illegality* which declared void an insurance policy issued to Respondent Wal-Mart, Inc. by Transit Casualty Company, now represented by Petitioner Receiver Lewis I. Crist. The Texas Property and Casualty Insurance Guaranty Association has paid certain claims made under this putatively void policy.

The Court of Appeals found that the doctrine of *pari delicto* applied to bar an insurance receiver from recovering on a policy of workers' compensation when, prior to receivership, the insurance company and the insured entered into an illegal premium arrangement. *Amicus curiae* requests permission to address the concept of *pari delicto* as applied to insurance company receivers, as such issue is of compelling national interest in the insurance industry. If the argument of the Texas Property and Casualty Insurance Guaranty Association is accepted, this argument would be dispositive of this case.

Respectfully submitted,

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PROOF OF SERVICE

I hereby certify that this motion and brief are being sent to the counsel for Petitioner and the counsel for Respondent as follows via certified mail on this day of March, 1989.

_____

KARL L. RUBINSTEIN

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QUESTION PRESENTED

Amicus Curiae Texas Property and Casualty Insurance Guaranty Association agrees that the Question Presented in the Petition filed by Petitioner adequately states the issue before this Court.

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AMICUS CURIAE BRIEF OF TEXAS PROPERTY AND CASUALTY INSURANCE GUARANTY ASSOCIATION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Amicus curiae, the Texas Property and Casualty Insurance Guaranty Association, submits this brief which respectfully requests this Court issue a writ of certiorari to review the judgment and opinion of the United States Court of Appeals for the Eighth Circuit, filed in the above-captioned proceeding on August 26, 1988.

OPINIONS

The statement of Opinions given in the Petition for a Writ of Certiorari correctly lists the opinions in issue in this case.

JURISDICTION

The statement of jurisdiction in the Petition for a Writ of Certiorari correctly states the basis for jurisdiction.

STATEMENT OF THE CASE

A correct Statement of the Case is given in the Petition for Writ of Certiorari. For the convenience of the Court, a brief encapsulation of that statement is given below.

This matter arises from the insolvency of Transit Casualty Company (hereinafter referred to as "Transit"). At issue in this particular case are over nineteen million dollars in premiums claimed due from Wal-Mart Stores, Inc. (hereinafter referred to as "Wal-Mart") to the Receiver of Transit. Of more importance than these millions of dollars, however, is the fact that the Eighth Circuit's opinion will have adverse ramifications throughout the entire insurance industry and will threaten the financial security of all American policyholders. Given the fact that the insurance industry involves the vital public interest and the fact that insurance is the cornerstone of the financial security of almost every American, this Court should address the issue in question.

The Eighth Circuit Court of Appeals has held that the claim of the Receiver of Transit against Wal-Mart, which admittedly has acted improperly and illegally, was barred. The rationale for the ruling was that the Receiver was in *pari delicto*

with Wal-Mart. The Eighth Circuit further found that the policy in issue was tainted with illegality and could not support an action for premiums. This ruling misunderstands and misapplies the true nature of the receiver and the true rights of the innocent policyholders and other creditors of the insolvent insurance company. If allowed to stand, it fundamentally threatens the entire basis of the insurance regulatory scheme.

NATURE OF APPLICANT'S INTEREST

The Texas Property and Casualty Insurance Guaranty Association (hereinafter referred to as "Texas Association") is a statutory association of insurers comprised of insurance companies licensed to do business in the State of Texas. The Texas Association was created pursuant to Texas Insurance Code Article 21.28-C, Section 14(A). The Texas Association is charged with several duties, including the duty to pay certain "covered claims" as defined in Texas Insurance Code Article 21.28-C, Section 5(2). "Covered claims" include the

> unpaid claim of an insured or third party liability claimant which arises out of and is within the coverage and not in excess of the applicable limits of an insurance policy . . . issued or assumed . . . by an insurer licensed to do business in this State, if such insurer becomes an 'impaired insurer'

as to certain claims of residents of Texas or claims arising as to property located in Texas.

In this case, Transit sold workers' compensation insurance to Wal-Mart. Upon the insolvency of Transit, claims putatively covered under the workers' compensation policy were made upon the Texas Association for payment of alleged "covered claims" within the meaning of Article 21.28-C, Section 5(2) of the Texas Insurance Code. Obviously, there can only be a covered claim if there was a policy and a loss occurred within the terms of the policy's coverage.

The foregoing notwithstanding, Wal-Mart has illegally avoided paying the statutorily mandated insurance premiums to Transit through the fraudulent acts of both Wal-Mart and an agent of Transit acting prior to receivership. At the same time, Wal-Mart asserts that the policies of insurance issued by Transit were void for illegality, due primarily to the fraud that Wal-Mart perpetrated while acting in concert with the Transit agent. The Eighth Circuit opinion has allowed the resulting unconscionable situation to stand.

In summary, Wal-Mart underpaid Transit in excess of $19,000,000.00 in terms of the statutorily mandated rate scheme. This underpayment, pursuant to the premium agreement, made the policy illegal. Now, various workers have suffered compensable losses, but the Transit receivership estate has insufficient funds to pay the claims, in part due to Wal-Mart's failure to pay the proper premium. The Eighth Circuit should have required Wal-Mart to pay the proper premium. Instead, the Eighth Circuit's decision rewards Wal-Mart for its duplicity and fraud by providing it with a windfall in excess of $19,000,000.00. Clearly, this is wrong. The other side of the coin is that but for the Texas Association and similar Associations in other states, the workers, for whose benefit every legislature in this country has enacted workers' compensation laws, are left without the statutory coverage. If the policy was indeed illegal and void, the Associations are not required to pay the workers' claims. Moreover, the Associations are prohibited from paying such claims because a covered claim can arise only out of a valid policy. To allow such a situation to exist and to allow such a burden to fall upon innocent policy beneficiaries, who are the precise persons the legislatures intended to protect with workers' compensation insurance, would be a travesty.

Since Wal-Mart has received the benefits of millions of dollars from the Texas Association, the Texas Association now is entitled to reimbursement of these sums. The Texas Association's right to recover these sums, however, may be clouded by the Eighth Circuit's finding, at 855 F.2d 1326 n.11, which

suggests that the receiver of an insolvent insurance company must be charged with any illegal acts committed by an insolvent insurance company. This footnote may be utilized by Wal-Mart to attempt to resist payment to the Texas Association. Beyond the Texas Association, however, and beyond this particular case, the Eighth Circuit's finding imperils all policyholders everywhere. This *amicus curiae* brief is filed in support of this Court's accepting jurisdiction over this case in light of the Eighth Circuit's holding and in view of this danger.

SUMMARY OF THE ARGUMENT

This court should review the finding that under the doctrine of *pari delicto* the receiver of an insolvent insurance company has no greater rights than did the insolvent insurance company to assert a premium claim. An insurance receiver is not acting as the company but is acting as the trustee of the trust fund made up of the assets of the insolvent company. These assets of the insolvent company are for the policyholders and other creditors of the insolvent in accord with the statutory priorities. The receiver is acting in a representative capacity for the true beneficiaries of the liquidation process. These beneficiaries are not in any way in *pari delicto* and are completely innocent. Given these circumstances the true parties in interest are innocent of any wrongdoing; they are strangers to any fraudulent actions and do not stand in *pari delicto* with Wal-Mart, Transit or its agent. To penalize these innocent parties and to reward the guilty parties is so far outside the fundamental principles upon which American jurisprudence is based as to be incomprehensible. This Court should not allow the Eighth Circuit decision to stand. Because the interests involved in this appeal transcend the context in which they arise, creating serious concerns about the due process rights of statutory insurance receivers and the parties for whom they act, this *amicus curiae* brief is filed to urge this Court to accept jurisdiction over this matter and to reverse the Eighth Circuit in respect to the *pari delicto* point.

THE ARGUMENT

I. THIS COURT SHOULD HEAR THIS CASE ON THE MERITS SINCE THE EIGHTH CIRCUIT DECISION MISAPPLIES THE DOCTRINE OF PARI DELICTO IN A FASHION WHICH FORECLOSES THE DUE PROCESS RIGHTS OF INSURANCE RECEIVERS

The states have, pursuant to their police power, enacted comprehensive regulatory schemes for the insurance industry. These enactments include detailed statutes which provide for insurance company liquidations through state court receiverships.

The instant case arises from a claim by an insurance insolvency receiver. The Plaintiff is Lewis R. Crist, statutory Receiver of Transit, an insolvent Missouri insurance carrier. The Defendant in the trial court was Wal-Mart, a major Arkansas corporation and a policyholder of Transit. This suit arises out of a premium claim for $19,946,038.20 by the Receiver against Wal-Mart, seeking to recover the proper premiums due under the policy. The policy in issue was a workers' compensation policy. Workers' compensation policies are subject to premium calculation on the basis of regulatory guidelines.

An underwriter who was a sub-agent of Transit negotiated with Wal-Mart's agent for a policy of workers' compensation. However, the underwriter and Wal-Mart together reported a reduced payroll calculation for Wal-Mart. The effect of this reduced payroll was to reduce the apparent amount due for premium by Wal-Mart since payroll figures are essential to calculation of the regulatory premium due. The policy was renewed, without rectification of the misstatement.

Transit's reinsurers later noted that Wal-Mart's losses under the policy were outside the parties' expectations. The

reinsurers refused to pay claims on the Wal-Mart policies. Wal-Mart commenced litigation on the policies and Transit counter-claimed for return of premiums in an amount based upon proper calculation under the regulatory manuals.

Transit was placed into liquidation, and the Receiver was substituted as Defendant in place of Transit. After an initial empaneling of a jury, trial was made to the bench, which rendered judgment for the Receiver.

The trial court held that the doctrine of *pari delicto* had no application since the principal transaction, the issuance of the policy, was not illegal. Thus, the trial court did not discuss the issue which this brief addresses. *See Wal-Mart Stores, Inc. v. Crist,* 664 F.Supp. 1242, 1268 (W.D. Ark. 1987), *rev'd,* 855 F.2d 1326 (8th Cir. 1988).

The Eighth Circuit reversed. *See Wal-Mart Stores, Inc. v. Crist,* 855 F.2d 1326 (8th Cir. 1988). The Eighth Circuit Court of Appeals held the Receiver for Transit could not recover the premiums since the parties were in *pari delicto* as to the premium reduction scheme.

In the course of its holding, the Eighth Circuit held that the statutory receiver of an insurance company may not assert claims which would be barred for illegality had the insurance company asserted them prior to insolvency. It is this holding that this *amicus curiae* seeks to challenge, and which justifies this Court's assertion of jurisdiction over the merits of this matter.

A. An insurance company receiver is not precluded from asserting a claim merely because the claim arises from illegality involving the insolvent insurance company.

The Eighth Circuit's *pari delicto* holding was not based upon actions of the Receiver, but rather upon acts of Transit committed prior to the receivership. The issue is thus presented as to what extent the receiver of an insurance company is bound

by the illegality of the company prior to receivership. The Eighth Circuit held that the receiver was tainted with any illegality committed by the company prior to receivership. This determination is incorrect and should be corrected by this Court.

Statutory insurance receivers are appointed as an exercise of the state's police power in regulating the business of insurance. In Missouri, the Director of Insurance may be appointed receiver of an insurance company on several alternative bases of impairment or hazard, including a finding that "further transaction of business will be hazardous to its policyholders or to its creditors or to the public". Mo. Rev. Stat. §375.560. Because a statutory receiver of an insurance company exercises authority pursuant to a state administrative system of insurance regulation, deference must be given to that receiver in the exercise of his duties. *Penn General Casualty Co. v. Pennsylvania*, 294 U.S. 189 (1935). The federal system has been loathe to intrude upon the state regulatory process. *AIMS Enterprises v. Muir*, 609 F. Supp. 257 (M.D. Pa. 1985).

In this case the threatened intrusion upon state regulatory systems is not an assumption of jurisdiction, but a holding which both directly contravenes established law as to the role of an insurance receiver and frustrates the fundamental purpose of the regulation of insurance, the protection of policyholders.

Unlike the ordinary private receiver, an insurance receiver is affected with the public interest. *Anderson v. Great Republic Life Ins. Co.*, 41 Cal. App. 2d 181, 106 P.2d 75 (1940); *Insurance Commissioner v. South Carolina Life & Health Ins. Guaranty Ass'n*, 267 S.C. 378, 228 S.E.2d 273 (1976); *Kueckelhan v. Federal Old Line Ins. Co.*, 69 Wash. 2d 392, 418 P.2d 443 (1966). As such, the statutory insurance receiver may bring actions to recover for illegal transactions in which the insurance company has engaged. *Gallin v. Burdick*, 152 Misc. 468, 273 N.Y.S. 456 (Sup. Ct. 1934), *aff'd*, 265 N.Y. 492, 193 N.E. 286 (1935).

This power to bring actions in the insurance receiver includes the power to act in a capacity representative of the creditors and policyholders of the company, as well as on behalf of the company itself. *Wheeler v. American National Bank,* 347 S.W.2d 918 (Tex. 1961). This power grants the insurance receiver enhanced powers compared with those of the company prior to receivership. *See Sheeran v. Sitren,* 168 N.J. Super. 402, 403 A.2d 53 (1979).

The case law has addressed expressly this power of the receiver in suits on policies which were allegedly illegal. In *McCarthy v. Knox,* 186 S.W.2d 832 (Tex. Civ. App.—Galveston 1945, writ ref'd w.o.m.), the policyholder raised a defense strikingly similar to that raised by Wal-Mart. The Texas Court of Civil Appeals rejected this defense in light of the nature of the receiver as a representative of creditors and policyholders. Similarly, in *English Freight Co. v. Knox,* 180 S.W.2d 633 (Tex.Civ. App.-Austin 1944, writ ref'd w.o.m.), a Texas Court of Civil Appeals upheld a receiver's premium claims notwithstanding an allegation of illegality.

There is a sound basis for this line of cases. This enhanced power in the receiver stems from his administration of the affairs of insolvent insurance companies for the benefit of creditors, the policyholders and the public. *Garris v. Carpenter,* 33 Cal. App. 2d 649, 92 P.2d 688 (1939). Missouri Revised Statutes 375.650 expressly states that the receiver holds the assets of the insolvent "for the use and benefit of the creditors and policyholders of such company and such other persons as may be interested in such assets." This statute and the other relevant authority makes it clear that the receiver does not act *qua* company but acts as the representative of policyholders and other creditors.

The fact that the instant case was tried under Arkansas law does not affect the validity of the authorities cited herein. The Arkansas Supreme Court has expressly recognized the public interest with which an insurance insolvency proceeding is

charged. *See Baldwin-United Corp. v. Garner,* 283 Ark. 385, 678 S.W.2d 754 (1984), *cert. denied,* 471 U.S. 1111 (1985). The principle urged by the Texas Association has been applied in the case of an FDIC receiver for a failed bank. In *D'Oench, Duhme & Co. v. Federal Deposit Ins. Co.,* 315 U.S. 447, 62 S. Ct. 676, 86 L.Ed. 956 (1942), this Court held that an FDIC receiver is not subject to all defenses available against the pre-receivership insolvent bank. This decision was based upon the fact that a wrongdoer should not be allowed to utilize an illegality defense since the policy of the National Banking Act was to prevent parties from taking actions which impair the capital of banks. Similarly, a state insurance regulator should be entitled to enforce the obligations of a wrongdoer such as Wal-Mart even when the insurance company was chargeable with participation of the wrong.

The basic concept behind insurance is that policyholders pay money to transfer risk from themselves to an insurance company. The insurance company expects and is paid to assume commercial and natural risks. The policyholders have absolutely no control and no knowledge of the day-to-day business operations of the insurance company. The policyholders are essentially at the mercy of the insurance company except to the extent the insurance laws protect their rights. It would be wrong to hold that these policyholders, who are truly strangers to the business operations of the company, stand in *pari delicto* with the company. The very point behind the doctrine of *pari delicto* requires that the parties to whom the doctrine applies actually stand together draped in some kind of guilt. Here, the innocent policyholders and creditors are guiltless.

In its opinion, 855 F.2d at 1335 n.11, the Eighth Circuit recognized the line of cases discussed above but refused to follow them, holding that no authority exists for the proposition that insurance receivers have powers similar to that of receivers of banks. This holding demonstrates the depth of the Court of

Appeals' misunderstanding of the nature of an insurance receiver.

If the Court of Appeals' ruling is allowed to stand, then no policyholder can rest assured that his or her policy means anything. Here, there was a statute which mandated the proper premium. This statute is deemed to have been incorporated into the contract and private parties cannot contract around the law. *See Connolly v. Pension Benefit Guaranty Corp.*, 475 U.S. 211, 106 S.Ct 1018 (1986); *Alpha Beta Food Markets, Inc. v. Retail Clerks' Union Loan 777*, 45 Cal.2d 764, 291 P.2d 433 (1955). This rule should result in a finding that the premium scheme, not the entire policy, was illegal. The result should be that the courts should read the statutorily mandated rates into the policy and force Wal-Mart to obey the law. The Court of Appeals has, instead, allowed the wrongdoers to profit.

In addition, if the Court of Appeals' opinion is allowed to stand, all policyholders would be constantly at risk that the actions of the insurance company would be asserted by the insurance company's fellow wrongdoers to avoid obligations to policyholders. The harshness of the Eighth Circuit's opinion is illustrated in the following example. Assume a large insurance company collects hundreds of millions of dollars from the public in premiums and then obtains reinsurance. This same company and its reinsurers enter into an illegal scam in connection with the reinsurance. The insurance company then becomes insolvent. Does the Eighth Circuit's opinion mean that the policyholders cannot, through the receiver, collect the reinsurance because the reinsurers and the company were in *pari delicto*? This cannot be the law in this country. However, application of such a rule would provide a windfall and immunity to all manner of insurance wrongdoers from the sweat of the brow of the American public. The *pari delicto* rule makes sense as an effort to curb the ability of conspirators to profit from the illegality which taints a transaction. However, it is illogical to apply that rule to an insurance receiver, who is, by

definition, acting only in a representative capacity for innocent parties. The cases involving receivers have never applied *pari delicto* to such a receiver, and this Court should review the erroneous decision of the Eighth Circuit to apply that doctrine in this context.

II. THE COURT OF APPEALS INVADED THE POLICE POWER OF THE STATE INSURANCE REGULATOR BY REFUSING TO ENFORCE THE PREMIUM LIABILITY

In addition to the foregoing concerns, the Eight Circuit's holding is in direct contravention to the established case law concerning illegal attempts to circumvent insurance regulations. In the case of *Bowen Motor Coaches, Inc. v. New York Casualty Co.*, 139 F.2d 332 (5th Cir. 1943), the court reformed a policy with an inaccurate account stated to accurately reflect the amount of premium due under the workers' compensation statutes. Such a reformation is a recognition of the state regulatory interests involved in the business of insurance. An insurance company is a highly regulated entity which must maintain reserves in accordance with law. The policyholders of an insurance company rely upon the insurance company to maintain its adequate reserves and to engage in pricing practices consistent with law. In this case, there is no question that Wal-Mart attempted to circumvent the rate regulations for workers' compensation policies. Accordingly, Wal-Mart should be held estopped to deny that it purchased a workers' compensation policy for which premiums would be due on a statutorily-calculated basis. Wal-Mart should not be permitted to escape its liabilities since it admittedly knew the basis on which premiums would have been calculated. To permit Wal-Mart to circumvent the statutory ratemaking scheme for workers' compensation premiums would be an invasion of the rights of the Transit Receiver in his capacity as trustee for the benefit of Transit's policyholders and creditors.

In this context, the *D'Oench* case also serves as a useful analogy. Indeed, it has been held that a party is *estopped* from denying the legality of a transaction where the plaintiff is the FDIC. *See F.D.I.C. v. Oehlert,* 252 N.W.2d 728 (Iowa 1977). *Oehlert* discusses extensively the federal policy preventing those dealing with banks from entering into transactions which result in a misstatement of surplus. A directly analogous argument may be made in the insurance insolvency context. In *Bonhiver v. Graff,* 311 Minn. 111, 248 N.W.2d 291 (1976), an alleged negligent tortfeasor contended that the fraud of the insurance company was the true cause of the tort. The Minnesota Supreme Court rejected this argument, holding an insurance receiver has enhanced rights due to his representation of creditors and policyholders. The application of this principle is even more clear in the case of a party whose actions amount to a fraud. *See Magnusson v. American Allied Ins. Co.,* 290 Minn. 465, 189 N.W.2d 28 (1971). As the Minnesota Supreme Court expressly recognized in *Magnusson,* an insurance company receiver is not bound by the fraud of the company he represents, since he represents not only that company but also the policyholders and creditors of the company.

The Eighth Circuit opinion flies in the face of the insurance regulatory scheme of the several states. The Court of Appeal's limitation on the rights of the insurance receiver is simply not supportable in light of either the case law, the statutory provisions, or the public policy of the states. Nevertheless, the decision injects an element of uncertainty into insurance receiverships which has been felt outside the confines of the facts of the case. This Court should grant certiorari in this case to prevent this newly-injected confusion from impairing the ability of the states' insurance regulators to proceed against the wrongdoers who contribute to the downfall of the insurance company and to protect the insurance-buying public.

This case is of concern to regulators in each of the nineteen states in which Wal-Mart's transaction occurred. This concern

arises from the fact that the insurance guaranty association (or other protective entity) in each state must confront the treatment of claims filed by Wal-Mart against their statutory coverage. For example, the Texas Association has paid claims on the basis of policies which Wal-Mart now asserts are void. Significantly, Wal-Mart may seek to utilize *pari delicto* as a weapon in the claim of the Texas Association for return of these payments under putatively void policies. This Court should clarify the application of the *pari delicto* doctrine through grant of a writ of certiorari in this case.

CONCLUSION

This case involves issues of national significance to insurance regulators. The Eighth Circuit's holding jeopardizes the rights of insurance receivers to collect assets of the estates of defunct insurance companies from the wrongdoers who caused dissipation of these assets. There are endless permutations of the kinds of illegal schemes that could be created. If such schemes can be used to void policyholder rights under policies and to avoid payment of premiums or reinsurance recoverables or other debts to the receiver, then the only fund the policyholders have to look to, the assets of the insolvent, will be gone. The capital and surplus requirements of the various state statutes will be meaningless. The Guaranty Associations will be powerless to pay claims on non-existent policies. Even if the Associations did pay, these funds are eventually derived from the citizens either in premium tax off-sets or in premium surcharges. What would be the point of insurance?

This Court should grant certiorari to remedy the error committed by the Eighth Circuit.

Respectfully submitted,

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